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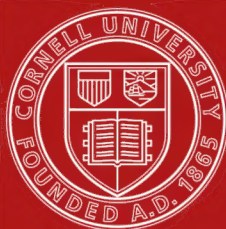
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CYCLOPEDIA
OF THE LAW OF
PRIVATE CORPORATIONS

1921 SUPPLEMENT

By **CLARK A. NICHOLS**

VOLUME X

CHICAGO
CALLAGHAN AND COMPANY
1921

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PREFACE

The first volume of Fletcher's *CYCLOPEDIA OF CORPORATIONS* was published in 1917. This supplement is designed to cover all the decisions relating to corporations up to 1921, including not only the decisions rendered by the federal and state courts in this country but also the late English and Canadian decisions. In addition, reference has been made to the late notes which have appeared in the several sets of annotated decisions, as well as to magazine articles relating to the law governing corporations.

The rulings relating to corporation law as set forth herein have been obtained by a page to page examination of the decisions handed down since the publication of this work, and include many statements of corporation law which cannot be found elsewhere.

In this supplement the law is classified under the identical section lines used in the original text, with the same section number, except where the matter is new and not included within any of the original section lines, in which case a new section line has been made and it is marked "[New]."

The supplement is intended for use after and not before the original text has been consulted. Having found the section in the original text where the question at hand is considered, all that is necessary is to turn to this supplement and ascertain if the section line as originally numbered is represented.

The reception which the *CYCLOPEDIA OF CORPORATIONS* has met, as indicated by its sale and by the many written and spoken words of commendation, indicates the profession's appreciation of the time, labor and money given to its preparation. It has fully sustained the only sure test of a law book—that of practical use. The publishers' confidence in the merits of the work is further justified by the numerous and steadily increasing citations and quotations of it by the courts, state and federal (not one of which has made an adverse comment or criticism), thus giving it the stamp of approval as an authoritative presentation of the law of corporations.

CLARK A. NICHOLS.

CHICAGO, September, 1921.

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PRIVATE CORPORATIONS

VOLUME X

CHAPTER 1

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§ 54. Person.

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II. DEFINITIONS AND ATTRIBUTES

§ 4. Leading definitions. A corporation is “an artificial entity existing only in contemplation of the law of its creation.”¹

§ 5. Attributes—In general. Capital stock is not an essential feature of a business corporation;² but it is held that the existence of capital stock and provisions for its transfer are an essential element of corporate existence, in case of a bank.³

§ 12. — Transfer of membership.⁴

III. THE CORPORATE FRANCHISE

§ 14. Primary.⁵

§ 15. Secondary.⁶

IV. DISTINGUISHED FROM OTHER FORMS OF ASSOCIATED BUSINESS

§ 16. Partnerships.⁷ A voluntary unincorporated association occupies an intermediate position between a partnership and a

¹ Joseph T. Ryerson & Son v. Shaw, 277 Ill. 524, 115 N. E. 650.

Many quotations of definitions of a corporation are set forth by Judge Ray in deciding that a lodge of Odd Fellows was a corporation within the bankruptcy statute, in *In re Carthage Lodge* No. 365, I. O. O. F., 230 Fed. 694, 700-702.

² State ex rel. Standard Tank Car Co. v. Sullivan, — Mo. —, 221 S. W. 728.

³ State v. Angle, 236 Fed. 644.

⁴ See § 25, *infra*.

⁵ See § 1148 et seq., *infra*.

⁶ See § 1156 et seq., *infra*.

⁷ Difference between corporations and partnerships, see *Haiku Sugar Co. v. Johnstone*, 249 Fed.

corporation.⁸ A Massachusetts Trust which is in effect no more than a partnership is not a corporation,⁹ unless so declared by statute.¹⁰

§ 17. Joint stock associations.¹¹ A "joint stock association" is not a corporation although it has most of its attributes.¹² It is not a citizen and its status in the federal courts must be judged by the citizenship of its members.¹³

§ 18. Societies, fraternities and clubs. Clubs are usually incorporated but generally in the form of nonstock corporations. A voluntary club is not a partnership, for the reason that the members are not associated for profit.

§ 19. Basic distinguishing features—Domestic associations. Calling an association a corporation, in a statute creating it, does not make it a corporation, since its character is to be determined by what it is and not by its name.¹⁴ A department of an incorporated college is not itself a corporation.¹⁵

V. CORPORATE ENTITY IN DEALING WITH THIRD PERSONS

§ 22. In general.¹⁶ A corporation is a distinct legal entity separate and apart from the individual stockholders who compose it.¹⁷ However, a corporation has no such separate entity

103; *W. T. Rawleigh Medical Co. v. Bunning*, — Neb. —, 176 N. W. 85.

Examples of "partnership associations," see *In re Caledonia Coal Co.*, 254 Fed. 742.

⁸ See *Brotherhood of Railroad Trainmen v. Cook*, — Tex. Civ. App. —, 221 S. W. 1049.

⁹ *Baker-McGrew Co. v. Union Seed & Fertilizer Co.*, 125 Ark. 146, 188 S. W. 571.

¹⁰ See § 6059, *infra*.

¹¹ Joint stock company distinguished from partnership, see *Haiku Sugar Co. v. Johnstone*, 249 Fed. 103.

¹² *Gifford v. Fargo*, 106 N. Y. Misc. 599, 176 N. Y. Supp. 568.

¹³ *Spencer v. Patey*, 243 Fed. 555.

¹⁴ *Middleton v. Texas Power & Light Co.*, 108 Tex. 96, 11 N. C. C. A. 873, 185 S. W. 556.

¹⁵ *Dubuque German College v. St. Joseph's College*, — Iowa —, 169 N. W. 405.

¹⁶ Corporate entity and international law, see article in 29 *Yale L. J.* 772-778, 815.

Domestic corporation as alien enemy because owned by subjects of an enemy state, see note on "Alien enemies" in *Ann. Cas.* 1918 C 709, 710.

¹⁷ *Com. v. Muir*, 170 Ky. 435, 186 S. W. 194.

as will permit it to act counter to the unanimous desire of its stockholders.¹⁸

The fact that the greater portion of the stock is held by one person does not affect corporate entity,¹⁹ nor does the fact that one person is the sole stockholder in a corporation.²⁰ But where an individual owns practically all the stock of a corporation and controls all its operations, the corporation and the individual are in proper cases regarded by the courts as one and the same.²¹ So in case of a one-man corporation, it is held he may do what he desires with the corporate assets, and no one but creditors can complain.²²

The theory of separate entity of a corporation is not disturbed by the ownership of a large part or all of its stock by another corporation.²³ A holding company owning a majority of the stock of another company is a separate entity just the same as a stockholder owning a majority of the stock of a corporation.²⁴ A "holding company has a separate corporate existence, and is to be treated as a separate entity, unless * * * such corporate existence is a mere sham, or has been used as an instrument for concealing the truth, or where the organization and control are shown to be such as that it is but an instrumentality or adjunct of another corporation."²⁵

Where two stockholders acquired all the stock under an agreement to distribute the net earnings twenty per cent as dividends and eighty per cent to one of the stockholders until his advances

¹⁸ *Pueblo Foundry & Machine Co. v. Lannon*, — Colo. —, 187 Pac. 1031.

¹⁹ *Macon v. Scandinavia Belting Co.*, 264 Pa. 384, 5 A. L. R. 1502, 107 Atl. 750.

The fact that nearly all the stock is held by one person does not destroy corporate entity; and his acts of usury, it seems, are not necessarily acts of usury of the corporation. *Salvin v. Myles Realty Co.*, 227 N. Y. 51, 6 A. L. R. 581, 124 N. E. 94, rev'g on other grounds 177 N. Y. App. Div. 886, 163 N. Y. Supp. 1131.

²⁰ *McMullen v. Westinghouse's Estate*, 259 Pa. 281, 103 Atl. 57.

²¹ *In re Wilson's Estate*, 85 Ore. 604, 167 Pac. 580, and see § 42, *infra*.

²² *Scales v. Holje*, — Cal. App. —, 183 Pac. 308.

²³ *Atchison, T. & S. F. Ry. Co. v. Weeks*, 248 Fed. 970, 978; *Kardo Co. v. Adams*, 231 Fed. 950, 964; *S. G. V. Co. of Delaware v. S. G. V. Co. of Pennsylvania*, 264 Pa. 265, 107 Atl. 721.

²⁴ *Com. v. Muir*, 170 Ky. 435, 186 S. W. 194.

²⁵ *Martin v. Development Co. of America*, 240 Fed. 42.

were repaid and then to the other until his advances were repaid, the existing corporate entity was not changed by such agreement into an incorporated partnership.²⁶

Similarity or even identity of corporate names "does not make identities of corporations formed under different sovereignties."²⁷

The fact that the government owns a majority of the stock of a corporation does not make it a department of the government.²⁸

§ 23. Contractual powers and obligations—In general.

A contract between stockholders does not bind the corporation.²⁹ So a purchaser of property from a corporation is not released from liability for the balance of the price by an agreement with a stockholder who, with his wife, owned all the stock of the corporation.³⁰ Where two or more persons agree that a corporation shall do a certain thing, which they can compel it to do because they hold a majority of the stock or otherwise, the corporation is not bound by their agreement but they bind themselves individually unless it is expressly agreed that the other party is looking to the corporation.³¹

But where all the stockholders make an agreement with one of them, and he acts in reliance on the contract, the other stockholders are estopped to deny the validity of the contract as binding the corporation.³² So it is held that the fact that mill properties were owned by a corporation does not limit the right of the sole stockholder to nominal damages for breach of a contract relating to such property, on the theory that a settlement and accounting of the affairs of the corporation would be necessary to establish actual damages.³³

²⁶ *Cuppy v. Ward*, 187 N. Y. App. Div. 625, 176 N. Y. Supp. 233.

²⁷ *Knott v. Fisher Vehicle Woodstock & Lumber Co. of Erin*, Arkansas, — Mo. App. —, 190 S. W. 378.

²⁸ *Commercial Pacific Cable Co. v. Philippine Nat. Bank*, 263 Fed. 218, and see § 2931, *infra*.

²⁹ *In re Northrop-Bell Oil & Gas Co.*, — Okla. —, 171 Pac. 1116; *Bell v. Northrop-Bell Oil & Gas*

Co., — Okla. —, 171 Pac. 1115.

³⁰ *Doughty v. Moors*, 38 Cal. App. 48, 53, 175 Pac. 273, 275.

³¹ *Morse v. Tillotson & Wolcott Co.*, 253 Fed. 340, 351, 1 A. L. R. 1485.

³² *Wootton Land & Fuel Co. v. Ownbey*, 265 Fed. 91.

³³ *Camp v. Gress*, 250 U. S. 308, 63 L. Ed. 997, *rev'g* in part 244 Fed. 121.

§ 24. — Agency. Stockholders who are not directors or officers are not liable to creditors of the corporation for the illegal or ultra vires acts of the corporation.³⁴

§ 25. — Acquisition and transfer of property—Title to property. Stockholders do not own the corporate property.³⁵ The title to corporate property is vested in the legal entity as such and not in its stockholders.³⁶ Corporate property belongs to the corporation and not to its stockholders, prior to distribution.³⁷ Furthermore, bonds held by a corporation are not the property of a stockholder although he owns all of the stock.³⁸

§ 26. — Transfers and conveyances. Stockholders, as distinguished from the corporation, cannot dispose of corporate assets.³⁹ They cannot, as individuals, sell corporate property.⁴⁰ Even though a stockholder owns practically all the stock, he cannot convey the corporate property nor use the assets for his own benefit;⁴¹ but the sole stockholder of a corporation which has forfeited its charter may convey the corporate real property, as president, and no one but creditors can complain.⁴² A stockholder has no interest in the good will of the corporation which he can sell.⁴³

§ 29. — Rights of action as to property.⁴⁴

§ 31. Torts.⁴⁵ Community as to officers, directors and stock of two companies does not of itself make one liable for acts

³⁴ Hoggan v. Price River Irrigation Co., — Utah —, 184 Pac. 536.

³⁵ Johnson v. Hay, — Kan. —, 190 Pac. 613.

³⁶ Com. v. Muir, 170 Ky. 435, 186 S. W. 194.

³⁷ United States Trust Co. of New York v. Heye, 224 N. Y. 242, 120 N. E. 645.

³⁸ First Nat. Bank of Memphis, Tennessee v. Towner, 239 Fed. 433.

³⁹ Burke Grain Co. v. Stinchcomb, — Okla. —, 173 Pac. 204.

⁴⁰ Robinson v. Taber, 198 Mich. 767, 165 N. W. 730.

⁴¹ Sanborn-Cutting Co. v. Paine, 244 Fed. 672.

⁴² Ginaca v. Peterson, 262 Fed. 904.

⁴³ Wylie v. Wylie Permanent Camping Co., — Mont. —, 187 Pac. 279.

⁴⁴ See § 4051 et seq., infra.

⁴⁵ Corporate identity of two corporations held shown so as to render one liable for the negligence of the other, in Lilikis v. Bossi, 205 Ill. App. 606.

of infringement committed by the other.⁴⁶ A general manager who owns nearly all the stock is not liable for personal injuries not resulting from his mismanagement, misconduct or negligence.⁴⁷

§ 33. Actions—General considerations.⁴⁸ If all the corporate property is leased with rent payable to the stockholders, the corporation may sue for the rent.⁴⁹ The fact that a corporation received part of the money sued for does not make stockholders liable therefor, since the corporation is a distinct entity from the shareholders.⁵⁰

§ 34. — Members as parties. A stockholder who owns the majority interest is not a necessary party to a suit against the corporation.⁵¹

§ 37. — Notice to members.⁵²

§ 38. — Admissions of members.⁵³

§ 39. — Residence and citizenship for jurisdictional purposes.⁵⁴

§ 40. Statute of frauds. A promise by a stockholder to answer for or pay a corporate debt is within the statute of frauds.⁵⁵ For instance, a promise by stockholders to be responsible for

⁴⁶ *Union Sulphur Co. v. Freeport Texas Co.*, 251 Fed. 634, 661, modified 255 Fed. 961, and see § 3340, *infra*.

⁴⁷ *Sterns Lumber Co. v. John H. Rice Co.*, 260 Fed. 434, and see § 2536, *infra*.

⁴⁸ See also §§ 2925, 2936, 4050, 4051, *infra*.

⁴⁹ *West End St. Ry. Co. v. Malley*, 246 Fed. 625.

⁵⁰ *Southern Cotton Oil Co. v. Knox*, 202 Ala. 694, 81 So. 656.

⁵¹ *General Inv. Co. v. Lake Shore & M. S. Ry. Co.*, 250 Fed. 160, *aff'g* 226 Fed. 976, and see § 3026, *infra*.

⁵² See § 2238, *infra*.

⁵³ See § 2175, *infra*.

⁵⁴ See § 2957, *infra*.

⁵⁵ *Richardson Press v. Albright*, 224 N. Y. 497, 8 A. L. R. 1195, 121 N. E. 362; *Friedlin v. Croekin*, 122 Va. 521, 95 S. E. 432. See also *Alexander v. Dove*, 230 Mass. 362, 121 N. E. 74, and § 4140, note 10 of vol. 6.

For note on "validity of oral promise by stockholder to pay debt of corporation," see 8 A. L. R. 1198.

rent of premises leased to the corporation is within the statute of frauds and hence must be in writing.⁵⁶

§ 41. Taxation. It is said that "this principle which recognizes the separate entity of a corporation distinct from its shareholders has more than ordinary significance when considered with reference to matters of taxation." And it was held that a holding company is not exempt from taxation on stock held in a foreign corporation merely because it owns a majority of such stock and itself fulfils the statutory requirement for exemption.⁵⁷

§ 42. Disregard of corporate entity—General statement.⁵⁸ In affirmance of the view that corporate entity will not be disregarded except in extreme cases, it is said that "except in cases where it is necessary to circumvent fraud, or in cases which proceed on the theory of estoppel, or those where it is sought to take possession of property ostensibly belonging to a corporation entirely controlled and owned by the principal debtor, for the purpose of protecting the creditors of the latter, as well as the former, it will be found that the instances are rare indeed where the general and settled rule of separate corporate entity is disregarded."⁵⁹ In any event, corporate forms should not be disregarded at the instance and for the benefit of one who has done the corporation a wrong.⁶⁰ Equity will disregard the form of a corporation and treat the parties as partners only where the interests of justice require and the facts warrant such action.⁶¹ However, the doctrine of corporate entity is not so sacred but that in condemnation proceedings by a corporation the court will look through corporate forms to ascertain the real party in interest.⁶²

⁵⁶ *Friedlin v. Croekin*, 122 Va. 521, 95 S. E. 432.

⁵⁷ *Com. v. Muir*, 170 Ky. 435, 186 S. W. 194.

⁵⁸ Disregarding corporate existence, see note in 1 A. L. R. 610-617, and see also 4 Minn. L. Rev. 219-227; 8 Calif. L. Rev. 435-437.

⁵⁹ *Peckett v. Wood*, 234 Fed. 833, 838.

⁶⁰ *Kardo Co. v. Adams*, 231 Fed. 950, 967.

⁶¹ *Thomashefsky v. Edelstein*, 192 N. Y. App. Div. 368, 182 N. Y. Supp. 707.

⁶² *Kardo Co. v. Adams*, 231 Fed. 950, 967.

§ 43. — Acts of members. Where the parties to an agreement for sale of stock by two to the other, own all the stock of a corporation, and there are no corporate debts, they may be treated as partners and the fiction of corporate entity disregarded, so far as the contract is concerned.⁶³ Where corporate officers agreed with one owning nearly all the stock, to not create any liabilities against the corporation, the corporation is not liable for money thereafter advanced to the corporation by such officers.⁶⁴

An interesting proposition is whether a corporation may recover of an insurance company for loss by fire where the fire was set by one who was the beneficial owner of practically all the corporate stock. The Illinois Supreme Court decided in the negative.⁶⁵

In case of a two-man corporation, it is generally held that corporate entity may be disregarded at least to the extent that contracts binding on the stockholders will be deemed binding on the corporation.⁶⁶ In some cases, in determining the rights of stockholders in a corporation controlled by two persons in equal degree, the law as applied to corporations is ignored and the parties held, as to their rights and obligations, as individuals.⁶⁷ But the rule that where two individuals own all the issued stock of a corporation, a court of equity will disregard the legal fiction that a corporation is a separate entity, where justice requires, is not applicable in all cases, as where there is an existing corporation prior to a purchase of its stock by two persons.⁶⁸ Where a corporation composed of husband and wife was a nominal thing created for the more con-

⁶³ *Komow v. Simplex Cloth-Cutting Mach. Co.*, 109 N. Y. Misc. 358, 179 N. Y. Supp. 682.

⁶⁴ *Newton v. Houston Hot Well Improvement Co.*, — Tex. Civ. App. —, 211 S. W. 960.

⁶⁵ *D. I. Felsenthal Co. v. Northern Assur. Co., Ltd.*, of London, 284 Ill. 343, 1 A. L. R. 602, 120 N. E. 268, *aff'g* 205 Ill. App. 610, and citing *Kirkpatrick v. Alleman Fire Ins. Co.*, 102 N. Y. App. Div. 327, 92 N. Y. Supp. 466 and *Meily Co. v. London & Lan-*

cashire Fire Ins. Co., 148 Fed. 683.

⁶⁶ *Commercial Security Co. v. Modesto Drug Co.*, — Cal. App. —, 184 Pac. 964.

⁶⁷ *Clark v. Schwaegler*, 104 Wash. 12, 175 Pac. 300; *Boothe v. Summit Coal Min. Co.*, 55 Wash. 167, 19 Ann. Cas. 1255, 104 Pac. 207.

⁶⁸ *Cuppy v. Ward*, 187 N. Y. App. Div. 625, 176 N. Y. Supp. 233, and see dissenting opinion of Justice Shearn.

venient handling of their property, it is no defense to an action for attorney's fees against husband and wife that there was no proof of employment by the corporation, since the corporate entity is properly ignored.⁶⁹ Where there are no creditors, and only three stockholders who have conducted the business more as a partnership than a corporation, a court of equity has power to disregard corporate entity and hold defendant stockholders liable to account to plaintiff stockholder directly, instead of to the corporation, where all the corporate stock has been sold and the proceeds are being distributed.⁷⁰ Corporate entity may be disregarded, and the controversy determined with reference only to rights as individuals, where two tenants in common of real estate incorporated with equal division of stock and directors between them; and in such a case neither tenant can obtain any advantage because of the corporate form adopted.⁷¹

§ 44. — Fraudulent acts. The doctrine of corporate entity should not be carried so far as to enable the corporation to become a means of fraud or a means to evade its responsibilities.⁷² Corporate entity will be disregarded where made an instrument of fraud⁷³ or where necessary to prevent fraud.⁷⁴ For instance, where parties engaged in business incorporate their business and are using the corporation as a cloak to accomplish some fraudulent purpose, equity will disregard the corporate form and enforce the individual liability of partners.⁷⁵ So equity will look through the fiction of a corporation formed for the purpose of accomplishing a fraud under the disguise of the fiction, although a transfer of property by a debtor to a corporation organized by him is not necessarily fraudulent.⁷⁶ Likewise, a corporate officer cannot claim protection for his personal

⁶⁹ *Clark v. Schwaegler*, 104 Wash. 12, 175 Pac. 300.

⁷⁰ *Gallagher v. Perot*, 112 N. Y. Misc. 717, 183 N. Y. Supp. 257.

⁷¹ *Cleveland-Cliffs Iron Co. v. Arctic Iron Co.*, 261 Fed. 15.

⁷² *J. J. McCaskill Co. v. United States*, 216 U. S. 504, 515, 54 L. Ed. 590.

⁷³ See *Winestine v. Rose Cloak*

& Suit Co., — Conn. —, 107 Atl. 500.

⁷⁴ *MacFadden v. Jenkins*, 40 N. D. 422, 169 N. W. 151.

⁷⁵ *Thomashefsky v. Edelstein*, 192 N. Y. App. Div. 368, 182 N. Y. Supp. 707.

⁷⁶ *Marine Nat. Bank v. Swigart*, 262 Fed. 854.

interests, in case of his fraud, on the theory that the entity which perpetrated the fraud was the corporation.⁷⁷ Where a corporation is owned and controlled by one person the rule of separate entity "can never be made use of for purposes of evading responsibility or as a means of distorting or hiding the truth or of covering up transactions."⁷⁸

It has been said that "it is only in case of bogus or dummy corporations, where it is necessary to disregard a pretended corporation in order to circumvent fraud, that the courts will ignore" the rule as to corporate entity.⁷⁹

§ 45. — Agency for parent corporation.⁸⁰ In determining corporate identity of two companies, the courts "look through corporate forms, and this disposition is shown with increasing firmness as the interests of justice require."⁸¹ Where stock ownership is resorted to, not for the purpose of participating in the affairs of a corporation in the normal and usual manner, but for the purpose of controlling a subsidiary company so that it may be used as a mere agency or instrumentality of the owning company, the courts will not permit themselves to be blinded by mere corporate forms but will, in a proper case, disregard corporate entity and treat the two corporations as one.⁸² As said by Judge Trieber in a federal case, "whatever may have been the views of the courts in the early days of corporate existence, when there were but few corporations, and they mostly confined to business of a quasi public nature, at this date courts,

⁷⁷ *Kay v. Piney Coal & Coke Co.*, — W. Va. —, 99 S. E. 501.

⁷⁸ *Searchlight Horn Co. v. American Graphophone Co.*, 240 Fed. 745.

⁷⁹ *Com. v. Muir*, 170 Ky. 435, 186 S. W. 194.

⁸⁰ See also § 22, *supra*.

Liability of parent company for debts of subsidiary, see article in 32 *Harvard L. Rev.* 424-428.

⁸¹ *Auglaize Box Board Co. v. Hinton*, 110 Ohio St. 505, 126 N. E. 881.

Two corporations may be in effect one, so as to cast the duty on

the lessor company of operating a railroad leased to the lessee company. *Brooks-Scanlon Co. v. Railroad Commission*, 144 La. 1086, 81 So. 727.

Where two companies are practically identical, one company may be held liable for the value of property delivered to the other. *Ivins v. Hub Machine Welding & Contracting Co.*, 68 Pa. Super. Ct. 370.

⁸² *Chicago, M. & St. P. R. Co. v. Minneapolis Civic & Commerce Ass'n*, 247 U. S. 490, 62 L. Ed. 1229, *aff'g* 134 Minn. 169, 158 N.

and especially courts of equity, will look behind the corporate fiction, and if it clearly appears that one corporation is mere'y the creature of another, the latter holding all the stock of the former, thereby controlling it as effectively as it does itself, it will be treated as the practical owner of the corporation when necessary for the purpose of doing justice."⁸³

An excellent statement of the rule as to corporate entity by Justice Grace of the North Dakota Supreme Court is as follows: "The time has passed, or at least is swiftly passing, when courts are confined, in their analysis, to the mere form and entity of the corporation. Courts will look upon the corporation as a legal entity until sufficient reason arises to look beyond the mere form and entity of the corporation. If the corporation is so organized that it can be used to defeat the rights of innocent parties, defeat public convenience, or cut off the right of redress, or of action against it or against other corporations of which it is, in effect, an agent, a court of equity will look

W. 817, and applying rule to ownership of terminal company by two railroad companies, so far as charging additional switching charges by terminal company was concerned.

Two corporations will not be regarded as separate and distinct entities, so as to prevent bankruptcy proceedings of the one being extended to the other, where not so regarded and treated in their operation by their directors, as where a manufacturer organizes two corporations and transfers to one the business and to the other the real estate and himself manages both as a part of the manufacturing business. In *re Looschen Piano Case Co.*, 261 Fed. 93.

Where a company organizes another company in another state, and manages and controls it for the purpose of transacting its business in such state, the parent company is liable on contracts or for acts of the subcorporation the same as if it had done business in

its own name. *John Church Co. v. Martinez*, — Tex. Civ. App. —, 204 S. W. 486.

The fact that the stockholders and directors of two corporations are entirely separate and distinct does not, so far as the public is concerned, make them absolutely independent concerns where the results and whole compass of their work and the effect of the organizations is to accomplish one purpose. *Advance-Rumely Thresher Co. v. Geyer*, 40 N. D. 18, 168 N. W. 731.

⁸³ *United States v. United Shoe Machinery Co.*, 234 Fed. 127, 141. To same effect, see *Dillard & Coffin Co. v. Richmond Cotton Oil Co.*, 140 Tenn. 290, 204 S. W. 758.

For an illustration of a case where the claim that a corporation was but an adjunct or agency of another corporation and therefore legal entity should be disregarded, was rejected, see *Peckett v. Wood*, 234 Fed. 833.

through the form of the corporation and examine the substance of it, and if several corporations are organized for a common purpose, it will look through the forms of all such corporations to the substance thereof, and the fact that several corporations are organized to carry out a common purpose will not prevent redress to an injured party, though the corporation which causes the injury or loss claims to have no connection with the general purpose for which the principal corporation is organized. Its legal entity will not alone protect it.”⁸⁴

In a federal case, Judge Hollister says that “from an examination of many decisions, we venture to say that no corporation acting within its powers has been held liable for the debts of another corporation legally organized, because it controlled such corporation by reason of ownership of its stock, or otherwise, except by reason of contract or on grounds of agency, or of estoppel, or because the controlled corporation has been used in such a way that the maintenance of its character as a separate and distinct entity would work injustice.”⁸⁵ The rule that distinct corporate existence will be disregarded where a subsidiary company is created simply as an “adjunct” or instrumentality of the holding company is subject to criticism if the word “adjunct” is used in its ordinary sense.⁸⁶

Identity of stock ownership, while not necessarily destroying separate corporate entity at least so far as capability of contracting between the two corporations is concerned, is important in considering the practical effect of intercorporate dealings, especially as bearing upon the duties of the common directors and the authority of the stockholders to control them.⁸⁷ Where a railroad company owned all the stock of an elevator company except qualifying shares for directors, and its acts were dictated and controlled by the railroad company, and the elevators were operated merely as a facility to the business of the railroad

⁸⁴ *Advance-Rumely Thresher Co. v. Geyer*, 40 N. D. 18, 168 N. W. 731.

⁸⁵ *New York Trust Co. v. Carpenter*, 250 Fed. 668, 674.

⁸⁶ *New York Trust Co. v. Carpenter*, 250 Fed. 668.

⁸⁷ *Corsicana Nat. Bank of Cor-*

sicana v. Johnson, 251 U. S. 68, 88, 64 L. Ed. 141.

Identity of stock ownership and close affiliation in management does not necessarily merge corporate identity. *Corsicana Nat. Bank of Corsicana v. Johnson*, 251 U. S. 68, 88, 64 L. Ed. 141.

company, the latter is liable for negligence of the elevator company.⁸⁸

Identity of officers of two corporations does not show identity of corporations.⁸⁹ Common directors and officers and stockholders does not make one corporation liable for infringement by another corporation.⁹⁰ The fact that two corporations have a common president, or in certain transactions acted one for the other, does not make them one and the same, but they are separate entities and liable alone for their separate contracts and acts.⁹¹ So a custom acted upon, or known as to two corporations, cannot make them one corporation, when the law created them two separate entities.⁹²

Although all the property of one corporation is transferred to another, the two are distinct legal entities.⁹³

Where one corporation conducts its own business through the instrumentality of another and in its name, the capital invested therein by the former cannot be treated as a loan to the latter as against the rights of third persons, nor can it share as a creditor in the assets of the insolvent subsidiary company.⁹⁴

Corporate entity should be disregarded so as to hold a reorganized corporation bound by an injunction against the old corporation, where the new corporation was controlled by officers, agents and stockholders who were bound by the injunction because of their relationship to the old corporation.⁹⁵

This rule as to disregarding corporate entity in case of several corporations was applied in an interesting case in North Dakota as follows: A company manufactured machinery. Another

⁸⁸ The Willem Van Driel, Sr., 252 Fed. 35.

⁸⁹ F. P. McKay Co. v. Savery House Hotel Co., 184 Iowa 260, 168 N. W. 295.

It follows that the fact that two corporations have directors or other officers in common does not preclude the right of one corporation to sue the other. G. W. Jones Lumber Co. v. Wisarkana Lumber Co., 125 Ark. 65, 187 S. W. 1068.

⁹⁰ Union Sulphur Co. v. Free-

port Texas Co., 251 Fed. 634, 661.

⁹¹ Planters' Oil Co. v. Gresham, — Tex. Civ. App. —, 202 S. W. 145.

⁹² Planters' Oil Co. v. Gresham, — Tex. Civ. App. —, 202 S. W. 145.

⁹³ Osgood v. Tax Commissioner, — Mass. —, 126 N. E. 371.

⁹⁴ S. G. V. Co. of Delaware v. S. G. V. Co. of Pennsylvania, 264 Pa. 265, 107 Atl. 721.

⁹⁵ Farmers Fertilizer Co. v. Ruh, 7 Ohio App. 430.

company was organized to sell the manufactured product. The latter company sold machinery on a warranty and turned over the note, given for the price, to the manufacturing company. In an action on the note, a breach of warranty was set up by the purchaser. It was held that the two corporations, although having different stockholders and officers, should be considered as one for the purpose of the action, and that the defense could be set up against the manufacturing corporation which was not a holder in due course.⁹⁶

VI. THE JURISTIC PERSON AND ITS INTERNAL RELATIONS

§ 50. Contracts.⁹⁷

§ 51. Transfers and conveyances.⁹⁸

§ 52. Actions. A corporation owning a controlling interest in another company may nevertheless sue the latter, without regard to motive.⁹⁹

VII. CONSIDERED AS A PERSON, RESIDENT OR CITIZEN

§ 54. Person. Whether the word "person" as used in a statute includes corporations is a matter of intent,¹ and depends largely on the context and the extent and purpose of the particular law.² In England, the Interpretation Act provides that the word "person," as used in criminal statutes, shall, unless the contrary intention appears, include a body corporate.³ Generally the word is construed as including corporations.⁴ For instance, a corporation has been held a "person" within statutes granting appeals;⁵ within an income tax statute;⁶ within stat-

⁹⁶ *Advance-Rumely Thresher Co. v. Geyer*, 40 N. D. 18, 168 N. W. 731.

⁹⁷ See § 4030 et seq., *infra*.

⁹⁸ See § 4032, *infra*.

⁹⁹ *City of Toledo v. Toledo Railways & Light Co.*, 259 Fed. 450.

¹ *State ex rel. Miller v. Reiter*, 140 Minn. 491, 168 N. W. 714.

² *Wallace v. Moore*, 178 N. C. 114, 100 S. E. 237.

³ *Mousell Bros., Ltd. v. London & North-Western Ry. Co.*, [1917] 2 K. B. 836.

⁴ *Wilson v. Israel*, 185 N. Y. App. Div. 816, 173 N. Y. Supp. 842.

⁵ *Patterson v. Baltimore City*, 127 Md. 233, 96 Atl. 458.

⁶ *State ex rel. Wisconsin Trust Co. v. Widule*, 164 Wis. 56, 159 N. W. 630.

utes of limitation;⁷ within a penal statute prohibiting pool halls in certain locations;⁸ within a statute authorizing any person or persons to act as relator in quo warranto proceedings;⁹ and within a statute giving a mechanic's lien to "all persons" performing labor, etc.¹⁰ On the other hand, it has been held that "any person," as used in a criminal statute, does not include corporations;¹¹ and that the provision in an 1887 statute that no "person" shall be surety on more than one license bond applies only to personal sureties, and not to corporation sureties, where corporation sureties were unknown in the state in 1887.¹²

A corporation is a "person" within the provision of the Federal Constitution relating to equal protection of the laws.¹³

For the reason that common sense requires the act to be so construed, the word "whoever" in the Espionage Act included corporations.¹⁴

§ 56. Citizen.¹⁵ Ordinarily a corporation is not a "citizen" within the meaning of statutory provisions.¹⁶ The North Carolina statute giving "any citizen," and "all persons" having the intent of becoming citizens, the right to make entries on vacant state land, does not apply to railroad companies, or at least does not authorize an entry except where required for the purposes of the road.¹⁷

⁷ *Atchison, T. & S. F. R. Co. v. Stamp*, 290 Ill. 428, 125 N. E. 381, railroad company.

⁸ *Caraway v. State*, — Ark. —, 219 S. W. 736.

⁹ *State ex rel. Northwestern Colonization & Improvement Co. of Chihuahua v. Huller*, 23 N. M. 306, 1 A. L. R. 170, 168 Pac. 528.

¹⁰ *Wood v. Isgrigg Lumber Co.*, — Ind. App. —, 123 N. E. 702.

¹¹ *Judge Lynch International Book & Publishing Co. v. State*, 84 Tex. Cr. 459, 208 S. W. 526.

¹² *State ex rel. Miller v. Reiter*, 140 Minn. 491, 168 N. W. 714.

¹³ *Bethlehem Motors Co. v. Flynt*, 178 N. C. 399, 100 S. E. 693.

¹⁴ *American Socialist Society v. United States*, 266 Fed. 212.

¹⁵ See also § 387 et seq., *infra*.

¹⁶ *Wallace v. Moore*, 178 N. C. 114, 100 S. E. 237.

¹⁷ *Wallace v. Moore*, 178 N. C. 114, 100 S. E. 237.

CHAPTER 2

CLASSIFICATION OF CORPORATIONS

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- § 81. — Public officers or public boards.
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- § 89. — “Transportation” and “railroad” corporations.
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- § 94. — “Banking” corporations—Trust companies.
- § 96. — “Insurance” corporations.
- § 97. — Building and loan associations.
- § 100. — “Charitable” and “benevolent” corporations.
- § 101. — “Religious” corporations.

§ 57. Aggregate and sole corporations.¹

§ 65. Public and private corporations—In general. Ordinarily the term “corporation” means private corporation,² and, as used in statutes, does not include municipal corporations;³ but the word “corporation” is sometimes used as including municipal corporations.⁴

¹ See § 22 et seq., supra, as to corporate entity.

² *Feemster v. City of Tupelo*, — Miss. —, 83 So. 804.

³ *Boulder v. Stewardson*, — Colo. —, 189 Pac. 1.

⁴ See *Guild v. City of Newark*, 87 N. J. Eq. 38, 99 Atl. 120.

§ 67. — Public corporations proper.⁵ A corporation is a public one where created for public purposes and no others.⁶ Acting in a proprietary capacity and in business matters, municipal corporations are governed by very much the same rules as private corporations.⁷ A municipal corporation is not a "private" corporation with respect to its public service functions, i. e., when carrying on a municipally owned public utility.⁸

§ 68. — Private corporations. A private corporation, as distinguished from a public one, is one formed for the benefit of its stockholders exclusively.⁹

§ 71. — Levee, drainage, reclamation and irrigation districts. An irrigation district is a public¹⁰ or quasi public corporation.¹¹ A drainage district was held in Florida to be in no sense a private corporation but a "public quasi corporation."¹² In another state it is held that a drainage district is not a private nor a municipal corporation but is a mere unincorporated governmental agency.¹³ Reclamation districts are, in strictness, not corporations at all but merely governmental agencies to carry out a specific purpose.¹⁴

§ 72. — Educational and charitable institutions. Cornell University is a private corporation, although aided by the state; and the state is not liable for negligence of one in the employ of the university department of agriculture.¹⁵

⁵ Other definitions of public corporations, see *Forbes Pioneer Boat Line v. Board of Com'rs*, — Fla. —, 82 So. 346.

⁶ *Forbes Pioneer Boat Line v. Board of Com'rs*, — Fla. —, 82 So. 346.

⁷ *Eau Claire Dells Improvement Co. v. Eau Claire*, — Wis. —, 179 N. W. 2.

⁸ *City of Pasadena v. Railroad Commission*, — Cal. —, 192 Pac. 25.

⁹ *Forbes Pioneer Boat Line v. Board of Com'rs*, — Fla. —, 82 So. 346.

¹⁰ *J. C. Engleman Land Co. v. Donna Irrigation Dist.*, — Tex. Civ. App. —, 209 S. W. 428.

¹¹ *American Rio Grande Land & Irrigation Co. v. Mercedes Plantation Co.*, — Tex. —, 208 S. W. 904.

¹² *Forbes Pioneer Boat Line v. Board of Com'rs*, — Fla. —, 82 So. 346.

¹³ *Strawberry Hill Land Corporation v. Starbuck*, 124 Va. 71, 97 S. E. 362.

¹⁴ *Argyle Dredging Co. v. Chambers*, — Cal. App. —, 181 Pac. 84.

¹⁵ *Green v. State*, 107 N. Y.

§ 73. Quasi public corporations. The possession of the franchise to be a corporation does not, of course, of itself, constitute the possessor a "public utility."¹⁶ An irrigation company, not requiring any special franchise, is held not a "public utility," in Louisiana;¹⁷ but in Texas they are held to be quasi public service companies.¹⁸ An ice company is a private corporation and not a quasi public one.¹⁹ A corporation formed to supply light, ice, water and power to a municipality is a quasi public corporation.²⁰ A fire insurance company is not a quasi public corporation although of a quasi public character.²¹ Cemetery corporations "are in a sense quasi public service corporations."²²

A mutual water company organized to deliver water to appropriators, without profit, is not a "public service" corporation, although it may be classified as a quasi public one.²³ Where practically all the water was devoted to use under water right certificates, although a small part was furnished a city and its inhabitants, the water company was not subject to regulation as a "public service" corporation.²⁴

§ 74. The United States, the states and territories as corporations. The state, although not a corporation in the strict sense of the term, may and does act as a corporate entity in a broad sense when it engages in the promotion and construction of public enterprises.²⁵ A state highway commission is not a municipal corporation.²⁶

Misc. 557, 176 N. Y. Supp. 681, and see §§ 3362, 3363, *infra*.

¹⁶ *State ex rel. Coco v. Riverside Irrigation Co.*, 142 La. 10, 76 So. 216.

Corporations subject to jurisdiction of public service commissions, see § 4379, *infra*.

¹⁷ *State ex rel. Coco v. Riverside Irrigation Co.*, 142 La. 10, 76 So. 216.

¹⁸ *Edinburg Irrigation Co. v. Paschen*, — Tex. Civ. App. —, 223 S. W. 329.

¹⁹ *Van Valkenburgh v. Ford*, — Tex. Civ. App. —, 207 S. W. 405.

²⁰ *Gulf Pipe Line Co. v. Las-*

ter, — Tex. Civ. App. —, 193 S. W. 773.

²¹ *National Union Fire Ins. Co. v. Dickinson*, 128 Ark. 367, 194 S. W. 254.

²² *Bliss v. Linden Cemetery Ass'n*, 90 N. J. Eq. 404, 107 Atl. 594.

²³ *Eldredge v. Mill Ditch Co.*, 90 Ore. 590, 177 Pac. 939.

²⁴ *Allen v. Railroad Commission*, 179 Cal. 68, 8 A. L. R. 249, 175 Pac. 466.

²⁵ *Indianapolis v. Indianapolis Water Co.*, — Ind. —, 113 N. E. 369.

²⁶ *Curtis & Hill Gravel & Sand*

§ 77. **Quasi corporations—Counties.** A county is only a quasi corporation, and is distinguishable from a private or municipal corporation.²⁷ The rules governing private corporations do not apply to counties.²⁸

§ 81. — **Public officers or public boards.** The Chicago Board of Trade, while incorporated, is a mere voluntary organization.²⁹

§ 84. **Statutory classification of corporations—In general.**³⁰ Telephone corporations are often held governed by statutes relating solely to “telegraph” companies.³¹ In some states, a telephone company cannot be created under that name but only as a telegraph company.³² A company whose purpose is to maintain an electric burglar alarm system is properly incorporated, in New York, under the “telegraph” act.³³

A town maintaining a free school system is an “educational corporation.”³⁴

Co-operative corporations are recognized as a separate class

Co. v. State Highway Commission,
— N. J. Eq. —, 111 Atl. 16.

²⁷ Breathitt County v. Hagins,
183 Ky. 294, 207 S. W. 713.

To same effect, see Mackenzie
v. Douglas County, 91 Ore. 375.
178 Pac. 350.

²⁸ Board of Com'rs v. Osborne,
104 Kan. 671, 180 Pac. 233.

²⁹ Turner v. Board of Trade of
Chicago, 244 Fed. 108.

³⁰ Canal companies, nature of
and duties, see State ex rel. West
v. Florida Coast Line Canal &
Transportation Co., 73 Fla. 1006,
L. R. A. 1917 F 776, 75 So. 582.

What constitutes “electrical
corporation,” as defined by Pub-
lic Service Commissions Law, see
Public Service Commission, Sec-
ond Dist. v. J. & J. Rogers Co., 184
N. Y. App. Div. 705, 172 N. Y.
Supp. 498.

A corporation is one “organized
for printing” where printing is
its principal business. Taylor-

Critchfield Co. v. Stuckart, 275 Ill.
129, 113 N. E. 895.

³¹ Cochranon Tel. Co. v. Public
Service Commission, 263 Pa. 506,
107 Atl. 23, distinguishing City of
Richmond v. Southern Bell Tele-
phone & Telegraph Co., 174 U. S.
761, 43 L. Ed. 1162.

Telephone business as “tele-
graph” business, see State Public
Utilities Commission ex rel. Chi-
cago Tel. Co. v. Postal Telegraph-
Cable Co., 285 Ill. 411, 120 N. E.
795.

³² Cochranon Telephone Co. v.
Public Service Commission, 70 Pa.
Super. Ct. 212.

³³ Holmes Elec. Protective Co.
v. Williams, 228 N. Y. 407, 127 N.
E. 315, rev'g on other grounds
181 N. Y. App. Div. 687, 168 N.
Y. Supp. 746.

³⁴ In re Guiteras' Estate, 113
N. Y. Misc. 196, 184 N. Y. Supp.
190.

of corporations by statutes in several states.³⁵ A stone quarry company is not a mechanical corporation.³⁶

§ 85. — Tests for ascertaining class of corporation. Classification of a corporation is to be determined by inspection of its charter.³⁷

§ 87. — “Mercantile” or “commercial” corporations. A corporation principally engaged in performing building or erection contracts is neither a “manufacturing” nor a “mercantile” corporation within the New York tax statutes.³⁸

§ 88. — “Manufacturing” corporations.³⁹ A corporation created to mine fire clay, etc., with the right to prepare for market and vend the product of the mines, was held not engaged in “manufacturing,” within certain tax statutes.⁴⁰

³⁵ See *McClure v. Co-Operative Elevator & Supply Co.*, 105 Kan. 91, 181 Pac. 573.

A co-operative association, such as the Minnesota legislature had in mind when authorizing incorporation of such associations, is a “union of individuals, commonly laborers, farmers or small capitalists, formed for the prosecution in common of some productive enterprise, the profits being shared in accordance with the capital or labor contributed by each.” *Mooney v. Farmers Mercantile & Elevator Co. of Madison*, 138 Minn. 199, 164 N. W. 804, quoting *Finnegan v. Noerenberg*, 52 Minn. 239, 18 L. R. A. 778, 38 Am. St. Rep. 552, 53 N. W. 1150.

Purpose of co-operative corporations and how different from ordinary business corporations, see *Chaffee v. Farmers’ Co-Operative Elevator Co.*, 39 N. D. 585, 168 N. W. 616.

A co-operative packing company, although its articles of incorporation were in form those of

a general corporation, was held to be a co-operative corporation so as to be entitled, under the 1917 statute in North Dakota, to file amended articles and thus become a co-operative corporation. *Equity Co-Operative Packing Co. v. Hall*, — N. D. —, 173 N. W. 796.

³⁶ *Graff v. Minnesota Flint Rock Co.*, — Minn. —, 179 N. W. 562.

³⁷ See § 118, *infra*.

³⁸ *People ex rel. Post & McCord v. Cantor*, 108 N. Y. Misc. 632, 178 N. Y. Supp. 579, which sets forth statutory definition of mercantile corporation.

³⁹ See also § 87, *supra*.

Definition of manufacturing corporation in tax statute, see *People ex rel. Post & McCord v. Cantor*, 108 N. Y. Misc. 632, 178 N. Y. Supp. 579.

Company as manufacturing corporation, see also *Ballard v. Hammond Coca-Cola Bottling Co.*, 147 La. 580, 85 So. 597.

⁴⁰ *Com. v. Welsh Mountain Mining & Kaolin Mfg. Co.*, 265 Pa. 380, 108 Atl. 722.

Operating a stone quarry is not of itself manufacturing.⁴¹ A corporation furnishing steel structures erected in place on realty, according to plans of engineers or architects, is neither a manufacturing nor a mercantile corporation.⁴²

§ 89. — "Transportation" and "railroad" corporations.⁴³

Whether street railroad companies are within the terms of statutes relating to "railroads" depends largely on the nature and terms of the particular statute.⁴⁴ Interurban electrics are not "railroads" as the term is used in some statutes,⁴⁵ although an interurban electric railway has been held a "railroad" within a remedial statute requiring railroads to fence their right of way.⁴⁶ Interurban railways may be within the terms of a statute relating to "railroads," although street railways are held not included.⁴⁷ An interurban railroad is not a "street railroad" as that term is used in some statutes.⁴⁸ A railway company operating its line on a private right of way is not a "street railway company."⁴⁹ A company whose tracks lie wholly within a single city and whose business is to transfer freights from one common carrier to another is a railroad company.⁵⁰ A logging railroad is a "railroad" within a statute defining them as all railways operated by steam;⁵¹ but tram or log roads

⁴¹ *Graff v. Minnesota Flint Rock Co.*, — Minn. —, 179 N. W. 562.

⁴² *People ex rel. Post & McCord v. Cantor*, 108 N. Y. Misc. 632, 178 N. Y. Supp. 579.

⁴³ Power company as transportation company, see *People ex rel. Cayuga Power Corporation v. Public Service Commission*, 226 N. Y. 527, 124 N. E. 105.

⁴⁴ *South Covington & C. St. R. Co. v. Com.*, 181 Ky. 449, 205 S. W. 603.

Electric street or suburban railway as within statute requiring "railroad" companies to fence their road, see *Muskogee Elec. Traction Co. v. Doering*, — Okla. —, 172 Pac. 793.

⁴⁵ *North Texas Transfer & Warehouse Co. v. State*, 108 Tex.

235, 191 S. W. 550. See *Stem v. Nashville Interurban Ry.*, 142 Tenn. 494, 221 S. W. 192.

⁴⁶ *Texas Elec. Ry. v. Barton*, — Tex. Civ. App. —, 213 S. W. 689.

⁴⁷ *Ft. Smith Light & Traction Co. v. Phillips*, 136 Ark. 310, 206 S. W. 453.

⁴⁸ *Bentler v. Cincinnati, C. & E. R. Co.*, 180 Ky. 497, L. R. A. 1918 E 315, 203 S. W. 199; *Koehn v. Public Service Commission*, 107 N. Y. Misc. 151, 176 N. Y. Supp. 147.

⁴⁹ *People v. Detroit United Ry.*, 207 Mich. 143, 173 N. W. 396.

⁵⁰ *Savannah River Terminals Co. v. Southern R. Co.*, 148 Ga. 180, 96 S. E. 257.

⁵¹ *Crawford v. Mullins Lumber Co.*, 110 S. C. 318, 93 S. E. 494.

used for private purposes are not "railroads" within taxing statutes.⁵²

§ 91. — "Business" corporations.⁵³

§ 92. — Corporations for "pecuniary profit."⁵⁴ The American Medical Association is not a corporation for pecuniary profit.⁵⁵ A by-law of a mutual co-operative corporation requiring members to pay three per cent of gross sales to the corporation when a sale is made to any one other than the corporation does not show that the corporation is one organized for pecuniary profit.⁵⁶

The right of a corporation to hold meetings outside the state may depend on whether the corporation is or is not one for pecuniary profit.⁵⁷

§ 93. — "Moneyed" corporations. A moneyed corporation is a corporation organized with the intention to accumulate wealth,⁵⁸ and includes an investment company.⁵⁹ A corporation making it a business to lend and borrow money, and deal in negotiable paper and securities, is a moneyed corporation.⁶⁰ A telephone company has been held a "moneyed corporation" within a forgery statute.⁶¹ "Moneyed institutions" are not confined to banks and savings institutions.⁶²

⁵² State v. Mississippi, A. & W. R. Co., 138 Ark. 483, 212 S. W. 317.

⁵³ "Business" corporations, as distinguished from "moneyed" corporations, under Maryland statutes, see Industrial Corp. of Baltimore City v. State Tax Commission of Maryland, 134 Md. 379, 106 Atl. 852.

Change of transportation corporation to business corporation by amendment of articles of incorporation, see People ex rel. Cayuga Power Corporation v. Public Service Commission, 226 N. Y. 527, 124 N. E. 105.

⁵⁴ What are corporations "organized for profit," see Von Baumbach v. Sargent Land Co.,

242 U. S. 503, 61 L. Ed. 460, rev'g 219 Fed. 31.

⁵⁵ People ex rel. Hoyne v. Grant, 283 Ill. 391, 119 N. E. 344, aff'g 208 Ill. App. 235.

⁵⁶ Ex parte Baldwin County Producers' Corporation, — Ala. —, 83 So. 69.

⁵⁷ People ex rel. Hoyne v. Grant, 283 Ill. 391, 119 N. E. 344, aff'g 208 Ill. App. 235.

⁵⁸ Grice v. Anderson, — N. C. —, 96 S. E. 222.

⁵⁹ Grice v. Anderson, — N. C. —, 96 S. E. 222.

⁶⁰ Grice v. Anderson, — N. C. —, 96 S. E. 222.

⁶¹ State v. Kennedy, 105 Kan. 347, 184 Pac. 734.

⁶² Industrial Corp. of Baltimore

§ 94. — “**Banking**” corporations—**Trust companies**.⁶³ A corporation is not necessarily a trust company because empowered to act as registrar and transfer agent of other corporations.⁶⁴ A trust company is not a banking corporation because it exercises some of the functions of a bank.⁶⁵

§ 96. — “**Insurance**” corporations.⁶⁶ Corporations engaged in guaranty and surety business are generally classified as “insurance” companies.⁶⁷ However, an incorporated fraternal benefit association is not an insurance company within the provisions of the Bankruptcy Act.⁶⁸ Fraternal benefit societies are, by statute, in many respects, exempted from the operation of the general insurance law and put in a class by themselves.⁶⁹

§ 97. — **Building and loan associations**.⁷⁰ Building and loan associations do not ordinarily come within statutes relating to banking.⁷¹

§ 100. — “**Charitable**” and “**benevolent**” corporations.⁷² An institution whose main purpose is educational is a charity

City v. State Tax Commission of Maryland, 134 Md. 379, 106 Atl. 852.

⁶³ Trust companies, statutory definition of, see Union Trust Co. v. Moore, 104 Wash. 50, 175 Pac. 565.

Trust company as similar to bank, see Skinner v. Schwab, 188 N. Y. App. Div. 457, 177 N. Y. Supp. 143.

⁶⁴ People v. National Security Co., 189 N. Y. App. Div. 38, 177 N. Y. Supp. 838.

⁶⁵ People v. National Security Co., 189 N. Y. App. Div. 38, 177 N. Y. Supp. 838.

⁶⁶ Creation of fraternal insurance companies in South Dakota, see Superior Lodge, Degree of Honor v. Van Camp, 40 S. D. 142, 166 N. W. 545.

A company engaged in indemnifying its members against loss from damages inflicted by automobiles is an “insurance” company.

Emerson v. Western Automobile Indemnity Ass’n, 105 Kan. 242, 182 Pac. 647.

⁶⁷ Greene v. National Surety Co., 186 Ky. 353, 217 S. W. 117, tax statutes.

⁶⁸ In re Grand Lodge A. O. U. W., 232 Fed. 199.

⁶⁹ Hollingsworth v. Supreme Council of Royal Arcanum, 175 N. C. 615, Ann. Cas. 1918 E 401, 96 S. E. 81.

⁷⁰ Nature of building and loan associations, and what are “like associations,” see Atlanta Loan & Saving Co. v. Norton, 149 Ga. 805, 102 S. E. 536.

Definition of building and loan association, see Holt v. Aetna Building & Loan Ass’n, 78 Okla. 307, 190 Pac. 872.

⁷¹ State v. Pelletier, 118 Me. 257, 107 Atl. 828.

⁷² Liability for torts, see § 3363, *infra*. Exemption from taxation, see § 4640, *infra*.

although it may have stock and stockholders.⁷³ Any corporation is within the term "charitable" or "educational," within the New York statute exempting them from the provisions of the inheritance tax, when, by its powers or usage, it is charged with administering charitable relief, and educating its people, even though it exercises other public functions.⁷⁴ A corporation is not necessarily a charitable one because created under the statute relating to churches, etc.⁷⁵ A purpose to secure either the passage or enforcement of laws believed to be for the public weal does not make a corporation having that for its object a benevolent or charitable one.⁷⁶ A local Y. M. C. A. is not necessarily a charitable corporation, at least in so far as it conducts a school.⁷⁷ A church club is not a "benevolent association" where it maintains a clubhouse, rents rooms, serves meals, secures positions for members, etc., and its only benevolent activities consist in securing positions for a few and furnishing a few free meals.⁷⁸ A fraternal benefit association is not necessarily a charitable corporation.⁷⁹ A corporation organized for mutual

Definition of a charitable organization, see *Congregational Sunday School & Publishing Society v. Board of Review*, 290 Ill. 108, 125 N. E. 7.

Humane Society, Home for Destitute and Crippled Children, and Visiting Nurse Association, held to be charitable corporations in *Skinner v. Northern Trust Co.*, 288 Ill. 229, 123 N. E. 289.

Methodist Episcopal Home, Masonic Home, and Odd Fellows' Home, as charities, see *In re Channon's Estate*, — Pa. —, 109 Atl. 756.

Odd Fellows' Homes as charitable corporations, see *In re Sharp's Estate*, 71 Pa. Super. Ct. 34.

Whether corporation formed by Catholic orders to give religious instruction to poor children, etc., was properly created as a "benevolent" corporation, see *Society of Helpers of Holy Souls v. Law*, 267 Mo. 667, 186 S. W. 718.

Property of charitable corporation as subject to mechanic's lien, see *Horton v. Tabitha Home*, 102 Neb. 677, 169 N. W. 2, 434.

⁷³ *Lightfoot v. Poindexter*, — Tex. Civ. App. —, 199 S. W. 1152.

Cornell University as charitable corporation, see *Hamburger v. Cornell University*, 99 N. Y. Misc. 564, 166 N. Y. Supp. 46.

⁷⁴ *In re Burnham's Estate*, 112 N. Y. Misc. 560, 183 N. Y. Supp. 539.

⁷⁵ *In re Dol's Estate*, — Cal. —, 187 Pac. 428.

⁷⁶ *Corbin v. American Industrial Bank & Trust Co.*, — Conn. —, 110 Atl. 459.

⁷⁷ *Susman v. Y. M. C. A.*, 101 Wash. 487, 172 Pac. 554.

⁷⁸ *Methodist Episcopal Church Baraca Club v. Madison*, 167 Wis. 207, L. R. A. 1918 D 1124, 167 N. W. 258.

⁷⁹ *McCarty v. Cavanaugh*, 224 Mass. 521, 113 N. E. 271.

assistance in case of sickness of members is not a "charitable or benevolent" corporation.⁸⁰ The Modern Woodmen of America is not a charitable organization but is an insurance corporation conducted on the assessment plan with certain social and charitable features.⁸¹

Whether a hospital is a charitable corporation is to be determined not only from its powers as set forth in its charter but also by the manner of conducting the hospital; and where, although organized for charitable purposes, it charged the same as other hospitals and had received no charity patients for thirteen years, it is not a charitable corporation.⁸² The fact that a hospital receives pay from a patient does not of itself affect its character as a charitable institution,⁸³ and a hospital may be a charitable corporation although most of its patients are pay patients and it conducts a nurse's training school.⁸⁴

§ 101. — "Religious" corporations.⁸⁵ The mere fact that a corporation is under the control of members of a particular church does not make it a religious corporation.⁸⁶

⁸⁰ *In re Dol's Estate*, — Cal. —, 187 Pac. 428.

⁸¹ *Morse v. Modern Woodmen of America*, 166 Wis. 194, Ann. Cas. 1918 D 480, 164 N. W. 829.

⁸² *Stewart v. California Medical Missionary & Benevolent Ass'n*, 178 Cal. 418, 176 Pac. 46.

Hospital as charitable corporation, see generally *O'Brien v. Physicians' Hospital Ass'n*, 96 Ohio St. 1, L. R. A. 1917 F 741, 116 N. E. 975.

⁸³ *O'Brien v. Physicians' Hospital Ass'n*, 96 Ohio St. 1, L. R. A. 1917 F 741, 116 N. E. 975.

⁸⁴ *Lutheran Hospital Ass'n of South Dakota v. Baker*, 40 S. D. 226, 167 N. W. 148.

⁸⁵ See also § 114, *infra*.

⁸⁶ *President & Council of Mt. St. Mary's College v. Williams*, 132 Md. 184, 103 Atl. 479.

CHAPTER 4

OBJECTS FOR WHICH CORPORATIONS MAY BE CREATED

§ 112. In general.

§ 114. Unlawful or injurious purposes.

§ 115. Attempt to incorporate under inapplicable statute.

§ 117. Number of purposes for which corporations may be formed.

§ 118. How character of a corporation is determined.

§ 119. Statement of objects in incorporation paper.

§ 120. Corporations for manufacturing or mechanical purposes.

§ 124. Corporations for benevolent, charitable, literary or educational purposes.

§ 126. Corporations for purposes of pecuniary profit.

§ 127. Corporations for owning or dealing in real estate.

§ 130. Corporations for the practice of law or medicine.

§ 112. In general.¹ A company was properly incorporated in New York under the general incorporation act of 1875 prohibiting incorporation thereunder for carrying on the business of banking or trust companies, although it was incorporated to transact the business of registrar and transfer agent of other corporations.² A company created to "operate" a long distance telephone line is within a statute relating to corporations created for the purpose of "constructing" and "maintaining" such a line.³

A corporation may be "legally" incorporated although one of the purposes for which it was incorporated was an unlawful corporate purpose.⁴

§ 114. Unlawful or injurious purposes.⁵ Where religious corporations are prohibited except to hold title to real estate for

¹ Right to organize a paid firemen's relief association in New Jersey, see *Westcott v. Passaic Paid Firemen's Relief Ass'n*, 91 N. J. L. 501, 103 Atl. 817.

² *People v. National Security Co.*, 189 N. Y. App. Div. 38, 177 N. Y. Supp. 838.

³ *Roaring Springs Town-Site Co. v. Paducah Tel. Co.*, 109 Tex. 452, 212 S. W. 147.

⁴ *Lewis v. Woodbury Dental Parlors Co.*, 106 N. Y. Misc. 78, 175 N. Y. Supp. 269.

⁵ A military company cannot be incorporated in New York except

churches, etc., a corporation cannot be formed solely for the purpose of imparting religious instruction to poor children.⁶ The West Virginia Constitution, so far as it prohibits the incorporation of "any church or religious denomination" does not apply to a society or other organization acting as an auxiliary thereto, such as a home missionary society.⁷

The act of taking out a corporate charter, although approved of by the state, cannot be made use of for purposes of fraud, but in such case equity will protect property rights of others.⁸ As against creditors of the grantor, a fraudulent grantee, such as a family corporation organized by a bankrupt when insolvent, stands in the grantor's place, and has no right, by way of subrogation, superior to that possessed by the grantor.⁹ Although there was fraud in the agreement for forming a corporation, the fact that a corporation was organized and issued its notes does not prevent a court from adjudicating rights between the parties themselves independently of the corporation.¹⁰ Whether the organization of a corporation was a fraud on the state because for a different purpose than that stated in the charter cannot be raised collaterally but only by the state in quo warranto proceedings.¹¹

An agreement between promoters to organize a corporation, acquire certain property, and finance the proposition, under which one is to secure the property and the others finance the proposition, the former to take one-fifth and the latter four-fifths of the stock, is not unlawful as against public policy although the par value of the stock was to be about four times the value of the property.¹²

Creditors dealing with a supposed corporation are chargeable with notice that the law prohibited such corporations.¹³

through the governor. *In re Long Beach Defense Guards*, 100 N. Y. Misc. 584, 166 N. Y. Supp. 459.

⁶ *Society of Helpers of Holy Souls v. Law*, 267 Mo. 667, 186 S. W. 718.

⁷ *Stump v. Sturm*, 254 Fed. 535, rev'g 239 Fed. 749.

⁸ *General Film Co. of Missouri v. General Film Co. of Maine*, 237 Fed. 64.

⁹ *In re Liller*, 253 Fed. 845.

¹⁰ *Goodspeed v. Law*, 260 Fed. 497.

¹¹ *La Salle v. Hamilton Nat. Bank*, 204 Ill. App. 518.

¹² *Queen v. Benesch*, 191 N. Y. App. Div. 83, 180 N. Y. Supp. 856.

¹³ *Davis v. Allison*, 109 Tex. 440, 211 S. W. 980.

§ 115. Attempt to incorporate under inapplicable statute. A corporation cannot be organized as a mutual co-operative society for farming and trucking, under the Alabama statutes, where the powers set forth in the charter are far in excess of those authorized by said statute.¹⁴

§ 117. Number of purposes for which corporations may be formed. In defining the purposes for which a corporation may be formed, the use of the word "or" will not be construed as limiting the creation of a corporation to a single one of the class of improvements mentioned, where to do so would be absurd.¹⁵ A college is not created for two distinct purposes, i. e., educational and religious, merely because the charter provides that it shall be under the charge of a certain religious denomination.¹⁶

A corporation cannot be organized in the District of Columbia for more than one object, and where its certificate expresses no primary object, and no such object is deducible from the language used in the certificate, but the certificate expresses a large number of objects, the charter is voidable.¹⁷

§ 118. How character of a corporation is determined. The nature and purpose of a corporation is to be found in its charter,¹⁸ and the articles of incorporation determine the class to which a corporation belongs.¹⁹ The purpose of a corporation,

¹⁴ Baldwin County Producers' Corporation v. Frishkorn, — Ala. App. —, 81 So. 862.

¹⁵ Bush v. State, 187 Ind. 339, 119 N. E. 417.

¹⁶ Lightfoot v. Poindexter, — Tex. Civ. App. —, 199 S. W. 1152.

"The mere fact that an institution of learning, operated under a charter granted by the state, is controlled and operated by a religious denomination, does not mean that it is organized and operated for religious purposes, when the charter plainly states that it is organized for educational purposes, and the facts show * * * that it is conducted and operated

for those purposes." Lightfoot v. Poindexter, — Tex. Civ. App. —, 199 S. W. 1152.

¹⁷ American Elementary Elec. Co. v. Normandy, 46 App. Cas. (D. C.) 329, 339.

¹⁸ Corbin v. American Industrial Bank & Trust Co., — Conn. —, 110 Atl. 459.

The purpose for which a company is organized must be ascertained by reference to the terms of its charter. Taylor-Critchfield Co. v. Stuckart, 275 Ill. 129, 113 N. E. 895.

¹⁹ Taylor-Critchfield Co. v. Stuckart, 275 Ill. 129, 113 N. E. 895; Bentler v. Cincinnati, C. & E.

as being within certain statutes, is to be determined solely from its charter,²⁰ and its essential nature cannot be affected by statements in its by-laws.²¹

§ 119. Statement of objects in incorporation paper.²²

§ 120. Corporations for manufacturing or mechanical purposes.²³

§ 124. Corporations for benevolent, charitable, literary or educational purposes.²⁴

§ 126. Corporations for purposes of pecuniary profit.²⁵

§ 127. Corporations for owning or dealing in real estate. In Illinois, a corporation cannot be created to acquire and hold a piece of real estate as an investment.²⁶ At common law a corporation may engage in the real estate brokerage business but it is otherwise under the Illinois statute although an Illinois corporation may engage in buying personal property.²⁷

§ 130. Corporations for the practice of law or medicine.²⁸

R. Co., 180 Ky. 497, L. R. A. 1918
E 315, 203 S. W. 199.

²⁰ *McIlvaine v. Foreman*, 292
Ill. 224, 126 N. E. 794.

²¹ *Canyon Creek Irrigation Dist.*
v. Martin, 52 Mont. 339, 159 Pac.
418.

²² See § 195, *infra*.

²³ See § 88, *supra*.

²⁴ See § 100, *supra*.

²⁵ See § 92, *supra*.

²⁶ *McIlvaine v. Foreman*, 292 Ill.
224, 126 N. E. 749.

²⁷ *Zehr v. Zehr*, 203 Ill. App.
584.

²⁸ See §§ 820, 822, *infra*.

CHAPTER 5

PROMOTERS

- § 132. Who are promoters.
- § 133. Rights and liabilities of promoters inter se.
- § 134. Relation of promoters to corporation and stockholders.
- § 135. Secret profits—In general.
- § 137. — Sale by promoter to corporation.
- § 138. — Qualification of general rules as to sales.
- § 139. — Joint and several liability.
- § 140. — Actions against promoters—Nature and form of remedy.
- § 141. — — Defenses.
- § 142. — — Parties.
- § 143. — — Limitations and laches.
- § 145. — — Burden of proof.
- § 146. — — Character and measure of relief.
- § 147. — — Commission from third person.
- § 150. Liability of corporation on promoters' contracts—In general.
- § 152. — Adoption or ratification of contracts.
- § 153. — Power to adopt or ratify ultra vires contracts.
- § 154. — Mode of adoption or ratification in general.
- § 156. — Implied adoption or ratification.
- § 158. Personal liability of promoters on contracts executed by them—In general.
- § 159. — Effect of adoption or ratification of contracts by corporation.
- § 161. Notice to or knowledge by promoters.
- § 164. Liability of corporation for services and expenses of promoters.
- § 165. Liability of promoters on failure to create corporation.
- § 166. Subscriptions to stock procured by promoters' fraud.

§ 132. Who are promoters. "Promoter" is a term, not of law but of business, summing up a number of operations familiar to the commercial word, generally those by which a corporation is brought into being.¹ Before incorporation, persons with whom a promoter makes a contract for their services are also promoters.²

¹ *Gates v. Megargel*, 266 Fed. 811, 816, approving *Whaley, etc., Co. v. Green*, 5 Q. B. Div. 109.

² *Van Zandt v. St. Louis Wholesale Grocer Co.*, 196 Mo. App. 640, 190 S. W. 1050.

§ 133. Rights and liabilities of promoters inter se.³ An agreement between promoters whereby one is to furnish a certain sum of money, where broken, creates a cause of action based on contract.⁴ Contracts of promoters are enforceable between them as stockholders after incorporation.⁵ Thus, agreements between incorporators before incorporation that the business is not to be disposed of except with the consent of all the parties, although never adopted by the corporation, are valid and enforceable between the parties.⁶ Promoters' contract between themselves whereby they agree to elect themselves as directors at a certain salary is not fraudulent, so as to vitiate the company's contract of employment with one of them, where he did not act as a director in making it.⁷

Where a corporation is formed to perpetrate a fraud, the promoters cannot enforce rights as against each other, since courts will not aid either party to an illegal contract.⁸ An attempt to incorporate by an evasive compliance with the statute is a fraud which cannot be enforced as between the parties.⁹

§ 134. Relation of promoters to corporation and stockholders.¹⁰

A promoter is not an "agent" of the proposed corporation,¹¹ although there is no question but that a promoter stands in a fiduciary relation to the corporation and to subscribers to stock therein.¹² It does not follow that "all moneys belonging to or

³ For note on "Validity and enforceability, inter se, of agreements between promoters of corporations," see L. R. A. 1918 E 833.

⁴ *Higgins v. Applebaum*, 186 N. Y. App. Div. 682, 174 N. Y. Supp. 807.

⁵ *Castorland Milk & Cheese Co. v. Shantz*, — N. Y. Misc. —, 179 N. Y. Supp. 131.

⁶ *Higgins v. Applebaum*, 186 N. Y. App. Div. 682, 174 N. Y. Supp. 807.

⁷ *Puller v. Royal Casualty Co.*, 271 Mo. 369, 196 S. W. 755.

⁸ *Allfather v. Schlicher*, 86 N. J. Eq. 1, 97 Atl. 491.

⁹ *Allfather v. Schlicher*, 86 N. J. Eq. 1, 97 Atl. 491.

¹⁰ Sale of stock by promoter at less than subscription price as binding on corporation, see § 567, *infra*.

Syndicate agreement between promoters and subscribers to bonds of a corporation to be organized, see *Jermyn v. Searing*, 225 N. Y. 525, 122 N. E. 706.

¹¹ *Reynolds v. Title Guaranty Trust Co.*, 196 Mo. App. 21, 189 S. W. 33; *Cator v. Commonwealth Bonding & Casualty Ins. Co.*, — Tex. —, 216 S. W. 140.

¹² *American Forging & Socket Co. v. Wiley*, 206 Mich. 664, 173

procured by a promoter, which may happen to have been handled or dealt with by him during the promotion of the corporation, are impressed with a trust in its favor."¹³ Promoters have no power to dispose of notes given for stock subscriptions until all the stock has been subscribed and the stockholders have elected officers.¹⁴ Promoters who own the property which is to be transferred to the corporation in exchange for corporate stock, or a portion of it, may agree among themselves as to the amount of stock that shall be issued for the property and how it shall be apportioned among them, and subsequent stockholders cannot complain.¹⁵

If a contract between promoters and the corporation was procured by fraud, the corporation may sue the promoter for damages or for an accounting or it can rescind the contract and recover back the consideration paid even from third persons to whom it was paid, where they received it with notice of the fraud. Such a contract is voidable and not void.¹⁶

In Illinois, money subscribed for capital stock of a life insurance company cannot be expended by promoters in forming the corporation.¹⁷

Where a promoter has not conveyed land to the corporation as agreed on, a stockholder cannot sue him directly to recover money paid for stock, but the action should be brought by the corporation.¹⁸

§ 135. Secret profits—In general. A promoter cannot speculate because of his position nor derive any secret advantage from it.¹⁹ Secret profits he cannot retain.²⁰ If promoters secure

N. W. 515; *Reynolds v. Title Guaranty Trust Co.*, 196 Mo. App. 21, 189 S. W. 33; *Goodman v. White*, 174 N. C. 399, 93 S. E. 906; *Ennis v. New World Life Ins. Co.*, 97 Wash. 122, 165 Pac. 1091.

¹³ *Reynolds v. Title Guaranty Trust Co.*, 196 Mo. App. 21, 189 S. W. 33.

¹⁴ *Pierik v. Mueller* 201 Ill. App. 108.

¹⁵ *Roberson v. Draney*, — Utah —, 178 Pac. 35.

¹⁶ *Arney v. Brittain & Co.*, 185 Iowa 1114, 171 N. W. 697.

¹⁷ *Lang v. Blocki*, 286 Ill. 91, 121 N. E. 163.

¹⁸ *Stewart v. King*, 85 Ore. 14, 166 Pac. 55.

¹⁹ *American Forging & Socket Co. v. Wiley*, 206 Mich. 664, 173 N. W. 515.

²⁰ *Gregg v. Megargel*, 248 Fed. 960; *North American Coal & Coke Co. v. O'Neal*, 82 W. Va. 186, 95 S. E. 822. See also *Gates v. Me-*

a greater number of shares than other stockholders in a new corporation organized to consolidate two existing corporations, the promoters must return the excess shares.²¹ The fact that the promoters were the only stockholders at the time securities were issued to them does not prevent such securities being considered secret profits as to subsequent purchasers of stock without notice of the fraud.²²

When promoters made an optional subscription to stock in the name of a trustee but with no intention of enforcing it if the company was not a success, but it was held out to the public as a binding subscription so as to be a fraud on future subscribers who would subscribe on the strength of the optional subscription, the transaction comes within the principle of the "secret profits" rule for the reason that the object was to reap a profit in the future at the expense of the other stockholders.²³

§ 137. — Sale by promoter to corporation. The secret profit rule is frequently applied to such sales.²⁴ Promoters are liable for secret profits where they purchase property for the purpose of the contemplated corporation and then sell it to the company at an advance without a full disclosure of the facts.²⁵ A promoter who transfers property to a corporation on a false statement that he paid more for it than he actually paid, is, it seems, liable to the corporation for the difference.²⁶ Dealings between a promoter and the corporation must be open and fair, and if he obtains a secret profit in turning over mining leases for stock of the company, the stock may be annulled.²⁷ Another

gargel, 266 Fed. 811; *Munson v. Fishburn*, — Cal. —, 190 Pac. 808.

For illustration of sale of safe to promoter at fictitious price, the promoter to pocket the balance, which was held not a sale to such promoter for resale so as to waive a clause as to retention of title until payment, see *Hall v. American Bankers' Safety Co.*, 116 Miss. 606, 77 So. 526.

²¹ *Lyons v. Webster*, 197 Ala. 654, 73 So. 337.

²² *Beal v. Smith*, — Cal. App. —, 189 Pac. 341.

²³ *Ennis v. New World Life Ins. Co.*, 97 Wash. 122, 165 Pac. 1091.

²⁴ *North American Coal & Coke Co. v. O'Neal*, 82 W. Va. 186, 95 S. E. 822.

²⁵ *Victor Oil Co. v. Drum*, — Cal. —, 193 Pac. 243.

²⁶ See *Hope Min. Co. v. Burger*, 37 Cal. App. 239, 174 Pac. 932.

²⁷ *Frame v. Mahoney*, — Ariz. —, 187 Pac. 584, citing *Fletcher's Cyc. Corp.* §§ 134, 135.

illustration: a promoter bought an interest in a furniture concern for \$4,000 and transferred it to the corporation for \$12,200, of which \$8,200 was in the corporate stock subscribed for at par. The promoter was also a director and his son and another were the other directors who between them owned all the capital stock. The trustee in bankruptcy was held entitled to recover \$8,200 on the subscription.²⁸ For a sale by promoters to the corporation to be valid, the corporation must be represented by an independent and impartial board of directors.²⁹

§ 138. — Qualification of general rules as to sales. There is no fraud where persons holding an option to buy land, which they paid \$500 for, formed a corporation and put in the land as worth \$3,000 more than the \$9,500 they had agreed to pay for it, since the option was of some value.³⁰

§ 139. — Joint and several liability. Promoters are jointly and severally liable for the full amount of secret profits where they all participated in the fraudulent scheme.³¹

§ 140. — Actions against promoters—Nature and form of remedy. A suit in equity may be maintained by a corporation against a promoter to recover stock or other property received by him in violation of his fiduciary duty.³² The remedy in equity is not precluded by the existence of a remedy at law, since the remedy at law is far less full and complete.³³

§ 141. — — Defenses. It is no defense to an action against promoters for secret profits in selling land to the corporation that the land was worth what it sold for.³⁴ The illegality of the organization of the corporation is not available to promoters as a defense.³⁵

²⁸ Goodman v. White, 174 N. C. 399, 93 S. E. 906.

²⁹ See Victor Oil Co. v. Drum, — Cal. —, 193 Pac. 243.

³⁰ Masberg v. Granville, 201 Ala. 5, 75 So. 154.

³¹ Victor Oil Co. v. Drum, — Cal. —, 193 Pac. 243.

³² American Forging & Socket

Co. v. Wiley, 206 Mich. 664, 173 N. W. 515.

³³ McNabb v. Tampa & St. P. Land Co., — Fla. —, 83 So. 90.

³⁴ Victor Oil Co. v. Drum, — Cal. —, 193 Pac. 243.

³⁵ American Forging & Socket Co. v. Wiley, 206 Mich. 664, 173 N. W. 515.

§ 142. — — Parties.³⁶ The corporation was held the proper party plaintiff where it was the one suffering the injury.³⁷ Ordinarily the corporation rather than the stockholders is the proper party to sue,³⁸ and the corporation may sue although the injury was to the individuals constituting the stockholders before the corporation was formed.³⁹

Where a promoter has in his possession shares of stock of the corporation, placed in his possession for the purpose of benefiting the corporation, and although he has never paid for the stock he denies the trust relation and asserts ownership of the stock, the corporation is so interested that it is the proper party to sue him in equity, and the promoter cannot deny the legality of the organization of the corporation.⁴⁰

§ 143. — — Limitations and laches.⁴¹ An action against promoters, for fraud, to recover secret profits, must be brought within the statutory period after discovery of the fraud; but it is only where the party defrauded should plainly have discovered the fraud except for his own inexcusable inattention that he will be charged with a discovery in advance of actual knowledge on his part.⁴²

§ 145. — — Burden of proof. The burden of showing a disclosure of the facts to subscribers, on a resale by promoters to the corporation at an advance, is on the promoters.⁴³

§ 146. — — Character and measure of relief. In equity that kind of relief will be granted which is best adapted to the situation, at the time it is applied for.⁴⁴

³⁶ Proper parties, see *North American Coal & Coke Co. v. O'Neal*, 82 W. Va. 136, 95 S. E. 822.

³⁷ *Jarvis v. Great Bend Oil Co.*, — Okla. —, 168 Pac. 450.

³⁸ *Masberg v. Granville*, 201 Ala. 5, 75 So. 154.

³⁹ *McNabb v. Tampa & St. P. Land Co.*, — Fla. —, 83 So. 90.

⁴⁰ *American Forging & Socket Co. v. Wiley*, 206 Mich. 664, 173 N. W. 515.

⁴¹ Laches held not a bar in *McNabb v. Tampa & St. P. Land Co.*, — Fla. —, 83 So. 90.

Delay of nearly a year after discovery of fraud held not laches barring action against promoters for secret profits, in *Victor Oil Co. v. Drum*, — Cal. —, 193 Pac. 243.

⁴² *Victor Oil Co. v. Drum*, — Cal. —, 193 Pac. 243.

⁴³ *Victor Oil Co. v. Drum*, — Cal. —, 193 Pac. 243.

⁴⁴ *American Forging & Socket*

§ 147. — — **Commission from third person.** A promoter empowered to buy a certain house and lot for a hospital at the lowest bid, agreed with the owner that the owner should pay the promoter a commission. Of course the corporation was entitled to recover the secret profit under the general rule as to secret profits.⁴⁵

§ 150. **Liability of corporation on promoters' contracts—In general.**⁴⁶ A promoter's contract cannot be enforced against the corporation unless and until adopted by it.⁴⁷ A corporation is not liable on a contract made with a promoter before its organization unless ratified by the corporation after its organization.⁴⁸ This rule as to nonliability of a corporation on contracts of promoters applies to services of attorneys rendered before incorporation.⁴⁹ A contract made with promoters before a Missouri corporation is authorized to commence business, under which it is to purchase real estate mortgages after it is authorized to do business, is not binding on the corporation.⁵⁰

§ 152. — **Adoption or ratification of contracts.** Contracts of promoters may be ratified or adopted by the corporation when organized,⁵¹ provided the contract is not illegal,⁵² so as

Co. v. Wiley, 206 Mich. 664, 173 N. W. 515.

⁴⁵ Waynesville Hospital v. Sutphen, 175 N. C. 94, 94 S. E. 663.

⁴⁶ Liability on promoters' contracts, see article in 3 Cornell L. Q. 292-298.

⁴⁷ International Agricultural Corporation v. Carpenter, 190 N. Y. App. Div. 359, 179 N. Y. Supp. 819; Wentworth v. Northern Producing Co., 172 N. Y. Supp. 342; Fuller v. Stout, — Okla. —, 166 Pac. 898; Cator v. Commonwealth Bonding & Casualty Ins. Co., — Tex. —, 216 S. W. 140.

A corporation is not bound by the promise of a promoter to pay for services. Speedograph Corporation v. Maier, — N. J. Eq. —, 111 Atl. 325.

⁴⁸ New Illinois Athletic Club v. Genslinger, 211 Ill. App. 220.

⁴⁹ Erd v. Rapid Transit Co., 206 Ill. App. 351.

⁵⁰ Missouri Fidelity & Casualty Co. v. Scott & Scott, — Okla. —, 178 Pac. 122.

⁵¹ Stone v. Walker, 201 Ala. 130, L. R. A. 1918 C 839, 77 So. 554; Smith v. Hutchinson Box Board & Paper Co., 101 Kan. 274, 166 Pac. 484.

Rule in Connecticut stated and discussed in United German Silver Co. v. Bronson, 92 Conn. 266, 102 Atl. 647.

⁵² Missouri Fidelity & Casualty Co. v. Scott & Scott, — Okla. —, 178 Pac. 122.

An adoption by a corporation of a contract made by its pro-

to make the corporation liable on the contract.⁵³ In regard to the Massachusetts rule to the contrary, it has been said: "Massachusetts holds that unless the elements of a new contract are present there can be no recovery. * * * Logically followed this would appear to eliminate the implied adoption which is in reality an application of the doctrine of estoppel." ⁵⁴ However, a company still in process of organization has no power, it seems, to assume a debt contracted by the promoters.⁵⁵

Adoption better expresses what takes place, since ratification presupposes a principal existing at the time of the agent's action.⁵⁶

"The law has placed certain safeguards about the adoption of the contract of the promoter in behalf of a corporation subsequently incorporated. It must be made within its corporate powers, for its benefit, be reasonable, and good faith must have surrounded its making and its adoption." ⁵⁷

A corporation may, in good faith, ratify or adopt agreements made or acts performed by the incorporators respecting organization expense, appearing to be reasonable and proper, when to do so in no way impairs either the capital or any surplus provided for by the charter.⁵⁸

Although attorney's services before incorporation were rendered in Missouri where the rule is that the corporation is liable for their reasonable value where impliedly accepted after incorporation, the law of Illinois governs the liability of an Illinois

motors to pay for services in shares of stock is not invalidated because the par value of the stock is greatly in excess of the value of the services. *Morgan v. Bon Bon Co.*, 222 N. Y. 22, 118 N. E. 205, rev'g 165 N. Y. App. Div. 89, 150 N. Y. Supp. 668.

⁵³ *Castorland Milk & Cheese Co. v. Shantz*, — N. Y. Misc. —, 179 N. Y. Supp. 131; *Wallace v. Eclipse Pocahontas Coal Co.*, 83 W. Va. 321, 98 S. E. 293; *McCullough v. Clark*, 81 W. Va. 743, 95 S. E. 787.

Construction of particular contract adopted by corporation, see

Wilson v. Mears, 105 Wash. 296, 177 Pac. 815.

⁵⁴ *United German Silver Co. v. Bronson*, 92 Conn. 266, 102 Atl. 647.

⁵⁵ *Reynolds v. Union Station Bank of St. Louis*, 198 Mo. App. 323, 200 S. W. 711.

⁵⁶ *United German Silver Co. v. Bronson*, 92 Conn. 266, 102 Atl. 647.

⁵⁷ *United German Silver Co. v. Bronson*, 92 Conn. 266, 102 Atl. 647.

⁵⁸ *Royal Casualty Co. v. Puller*, 194 Mo. App. 588, 186 S. W. 1099.

corporation where any implied acceptance must have occurred in Illinois.⁵⁹

Adoption by the corporation of contracts of promoters carries with it the obligations and burdens imposed by the contract.⁶⁰

If stock is to be delivered in pursuance of a promoter's contract with a third person, adopted by the corporation, for a transfer of property to the corporation, the contract may be specifically enforced against the corporation.⁶¹

§ 153. — Power to adopt or ratify ultra vires contracts.⁶²

§ 154. — Mode of adoption or ratification in general. The ratification of acts of promoters need not be in writing, since it is an original undertaking not within the statute of frauds.⁶³

A resolution passed at a stockholders' meeting merely commending and approving generally all the acts of the promoters does not amount to a ratification of a contract made by the promoters.⁶⁴

§ 156. — Implied adoption or ratification. The adoption or ratification of acts of promoters may be implied instead of express, as by acceptance of benefits,⁶⁵ with full knowledge of the

⁵⁹ *Erd v. Rapid Transit Co.*, 206 Ill. App. 351.

⁶⁰ *City of Belfast v. Belfast Water Co.*, 115 Me. 234, L. R. A. 1917 B 908, 98 Atl. 738.

⁶¹ *Wallace v. Eclipse Pocahontas Coal Co.*, 83 W. Va. 321, 98 S. E. 293.

⁶² For a general review of the law on this subject, as decided by the Connecticut courts, see *United German Silver Co. v. Bronson*, 92 Conn. 266, 102 Atl. 647.

⁶³ *Hart-Toole Furniture Co. v. Shahan*, — Tex. Civ. App. —, 220 S. W. 181, citing *Fletcher's Cyc. Corp.* § 154.

⁶⁴ *Missouri Fidelity & Casualty Co. v. Scott & Scott*, — Okla. —, 178 Pac. 122.

⁶⁵ *Stone v. Walker*, 201 Ala. 130, L. R. A. 1918 C 839, 77 So. 554.

If a corporation, when formed, accepts the benefits of previous contracts made in its name or for its benefit, it is liable thereon. *Plains Iron Works Co. v. Haggott*, — Colo. —, 188 Pac. 735.

Employment of servants by a promoter is ratified by permitting them to remain in their position after incorporation of the company and the acceptance of the services. *Outing Kumfy-Kab Co. v. Ivey*, — Ind. App. —, 125 N. E. 234.

Promoters' contracts, evidenced by an agreement to merge various firms, are binding on the corporation on its acceptance of the bene-

facts,⁶⁶ or payments on the contract.⁶⁷ Adoption may consist of the fact that the directors (the same persons who made the contract in the first place) recognize the contract and accept the services rendered thereunder for a number of years.⁶⁸ After a water company has acted for 30 years under the provisions of a promoters' contract, it cannot claim that it never adopted the contract.⁶⁹

Where the organizers of a corporation become its stockholders, and they, after the creation of the corporation, as its officers, accepted the benefit of services contracted for by them as promoters, there is an adoption of the contract by the corporation.⁷⁰

§ 158. Personal liability of promoters on contracts executed by them—In general.⁷¹ Where a contract with promoters is made solely on behalf of, and the credit extended solely to, the corporation then in process of formation, and which shortly thereafter secures its charter, the promoters are not personally liable on the contract.⁷² Incorporators who purchased property for the corporation a few days before the completion of incorporation,—the seller understanding that the purchase was by the corporation,—are not personally liable because of a slight misnomer in signing the corporate name to notes, etc.,

fits thereof. *Nannizzi v. Caprile*, — Cal. App. —, 185 Pac. 673.

The benefit a corporation received from services rendered is sufficient consideration to support an adoption of the promoter's contract for such services. *Hart-Toole Furniture Co. v. Shahan*, — Tex. Civ. App. —, 220 S. W. 181, citing *Fletcher's Cyc. Corp.* p. 338.

⁶⁶ *Fairbanks, Morse & Co. v. Merchants' & Consumers' Market House Ass'n*, 199 Mo. App. 317, 202 S. W. 596; *Moriarity v. Meyer*, 21 N. M. 521, L. R. A. 1916 E 1165, 157 Pac. 652.

⁶⁷ *Galdieri & Co. v. Arthur Waist Co.*, 98 N. Y. Misc. 612, 163 N. Y. Supp. 154.

⁶⁸ *Expansion Gold Mining &*

Leasing Co. v. Campbell, 62 Colo. 410, 163 Pac. 968.

⁶⁹ *City of Belfast v. Belfast Water Co.*, 115 Me. 234, L. R. A. 1917 B 908, 98 Atl. 738.

⁷⁰ *Morgan v. Bon Bon Co.*, 222 N. Y. 22, 118 N. E. 205, rev'g 165 N. Y. App. Div. 89, 150 N. Y. Supp. 668.

⁷¹ Construction of lease under which personal liability of promoters was to end when a certain sum in cash was paid into the treasury of the corporation, as to whether payment in property was payment in cash, see *Ivy v. Binswanger & Co.*, 141 Tenn. 568, 214 S. W. 74.

⁷² *Carle v. Corhan*, — Va. —, 103 S. E. 699.

for the price.⁷³ If promoters agree that the corporation shall do a certain thing which they can compel it to do because they control it, the corporation is not bound by their agreement but they bind themselves individually unless it is expressly agreed that the other party is looking to the corporation and not to the promoters.⁷⁴ Incorporators are not liable individually merely because the corporation has not assets sufficient to satisfy a claim.⁷⁵

If the promoters agree to save a subscriber to stock from loss on the investment, he may sue them for the amounts advanced with interest where the stock becomes worthless.⁷⁶

§ 159. — Effect of adoption or ratification of contracts by corporation. There is a novation where it is so agreed by all the parties.⁷⁷

§ 161. Notice to or knowledge by promoters. Notice to the promoters is notice to the corporation in some cases. Thus notice to them of the provisions of a contract made for and on behalf of the corporation is notice to the corporation accepting the benefits thereof.⁷⁸

§ 164. Liability of corporation for services and expenses of promoters.⁷⁹ The law relating to compensation of promoters is laid down as follows by the Connecticut Court of Errors: "Unless the charter or statute law otherwise provides, and the corporation does not, subsequent to the incorporation, obligate

⁷³ Carle v. Corhan, — Va. —, 103 S. E. 699.

⁷⁴ Morse v. Tillotson & Wolcott Co., 253 Fed. 340, 1 A. L. R. 1485.

⁷⁵ J. W. Williams Co. v. Leong Sue Ah Quin, — Cal. App. —, 186 Pac. 401.

⁷⁶ Vinton v. Pratt, 228 Mass. 468, L. R. A. 1918 D 343, 117 N. E. 919.

Contract of promoter to indemnify against loss a subscriber to stock who gave a note is a valid and enforceable one. Anderson v. First Nat. Bank, — Tex. Civ. App. —, 191 S. W. 836.

⁷⁷ Burress v. Montgomery, 23 Ga. App. 590, 99 S. E. 143.

⁷⁸ Wallace v. Eclipse Pocahontas Coal Co., 83 W. Va. 321, 98 S. E. 293.

⁷⁹ That embryo insurance company has no power to pay commissions for selling stock, in Missouri, see Reynolds v. Whittemore, — Mo. —, 190 S. W. 594.

Construction of contract as to commissions for sale of stock, see Kingsbury v. Riverton-Wyoming Refining Co., — Colo. —, 192 Pac. 503.

itself to pay, it is under no obligation to pay for the services or expenses incurred in promoting its incorporation. * * * Where, as in this case, there is no contract, but simply service performed and expenses incurred in the incorporation, before the corporation should be charged with their adoption, they should be found to be of corporate benefit, reasonable in amount, and incurred under circumstances which show that they were not in fact, nor intended to be, mere gratuities. The corporation has no choice in determining upon the acceptance of these, hence it cannot be held by retaining the benefits to have estopped itself from denying its adoption of them and its liability to pay for them. The acts and conduct from which the adoption by a corporation can be inferred are those only which it may voluntarily accept or reject.”⁸⁰ Generally a corporation is not liable for services of promoters, and the mere fact of incorporating and proceeding as a corporate body does not show an acceptance of the benefits of their services in obtaining subscriptions to stock.⁸¹

A contract for compensation for procuring stock subscriptions is not invalid, under the Texas statute, where the compensation is not to be paid from the amounts received from subscribers.⁸² Money subscribed for capital stock of an insurance company cannot, in Illinois, be expended in payment of promotion expenses.⁸³ An agreement to pay a promoter money and stock for procuring persons to organize a corporation to take over property cannot be specifically enforced where there is a want of consideration.⁸⁴

A corporation may, where there is no statute to the contrary, issue stock in payment of the services of promoters.⁸⁵ Where

⁸⁰ *United German Silver Co. v. Bronson*, 92 Conn. 266, 102 Atl. 647.

Ratification by stockholders and others of payment of promotion expenses, see *Liggett v. Roanoke Water Co.*, — Va. —, 101 S. E. 55.

⁸¹ *Van Zandt v. St. Louis Wholesale Grocer Co.*, 196 Mo. App. 640, 190 S. W. 1050, reviewing the question of liability at length.

⁸² *Thannish v. Brewton Trans-*

fer & Auto Co., — Tex. Civ. App. —, 220 S. W. 300.

⁸³ *Lang v. Blocki*, 286 Ill. 91, 121 N. E. 163.

⁸⁴ *Plains Iron Works Co. v. Haggott*, — Colo. —, 188 Pac. 735.

⁸⁵ *United German Silver Co. v. Bronson*, 92 Conn. 266, 102 Atl. 647.

If a corporation votes to deliver a certain amount of stock to a promoter for his services, another

a corporation sues promoters to recover the par value of stock issued to them for their services, it thereby recognizes the issuance of such stock and waives the objection that the stock could not be issued except for cash.⁸⁶ If a promoter is promised shares of stock in case the corporation was organized, he cannot recover the value thereof where the corporation was never organized, unless the failure to organize was due to the acts of the persons making the promise.⁸⁷ If a promoter is to receive for his services shares of stock, but the number of shares is not specified, and the parties cannot agree as to the amount of stock to be paid him, he may recover in money the reasonable value of his services.⁸⁸

A promoter may be paid any amount the parties in interest agree upon.⁸⁹ He may be allowed commissions on his own subscription to stock as well as on subscriptions of third persons.⁹⁰

A promoter who betrays his trust and diverts funds received for the proposed corporation forfeits his right to compensation for services.⁹¹

A contract to organize a company, in consideration of stock, means an incorporated company.⁹²

In settling his account for expenditures, a promoter cannot represent both himself and the corporation.⁹³

§ 165. Liability of promoters on failure to create corporation.⁹⁴ Promoters or incorporators who receive payments of subscriptions to stock of a proposed corporation are personally liable for the return of the money paid, in case of failure to

stockholder cannot complain.
Decke v. Baker, 201 Mich. 608,
 167 N. W. 908.

⁸⁶ *United German Silver Co. v. Bronson*, 92 Conn. 266, 102 Atl. 647.

⁸⁷ *Gray v. Bullen*, 50 Utah 270,
 167 Pac. 683.

⁸⁸ *Winch v. Warner*, — N. Y. App. Div. —, 174 N. Y. Supp. 819.

⁸⁹ *Decke v. Baker*, 201 Mich. 608, 167 N. W. 908.

⁹⁰ *Royal Casualty Co. v. Puller*, 194 Mo. App. 588, 186 S. W. 1099.

⁹¹ *Venie v. Harriet State Bank*, — Minn. —, 178 N. W. 170.

⁹² *Kennedy v. Burns*, — W. Va. —, 101 S. E. 156.

⁹³ *Lake Harriet State Bank of Minneapolis v. Venie*, 138 Minn. 339, 165 N. W. 225.

⁹⁴ Measure of damages for failure to form corporation in which plaintiff was to receive a certain amount of stock for a cash payment and devote his time to the business, see *Brown v. Owings*, 112 S. C. 499, 101 S. E. 38.

perfect the corporation.⁹⁵ If money is paid promoters for stock, and the attempt to form the corporation is abandoned, the subscribers to stock may sue the promoter for money had and received.⁹⁶ If the agreement of subscription to stock provides that five dollars a share shall be used partly for organization purposes, and the project of incorporation fails, the promoters are personally liable to subscribers for any sums used for organization expenses in excess of the five dollars a share.⁹⁷

§ 166. Subscriptions to stock procured by promoters' fraud.

The rule as to fraud applies to misrepresentations by a promoter where the contract has been adopted by the corporation.⁹⁸ A promoter who knowingly issues or sanctions the circulation of a false prospectus containing untrue statements of material facts inducing a purchase of stock in the corporation is liable to a purchaser injured thereby, whether or not the promoter knew of the falsity of the statements.⁹⁹ An incorporator who signs the articles of incorporation is liable to a creditor who relies on false statements in such articles as to the value of property taken in payment for capital stock and as to the amount of stock paid up, after the corporation is insolvent.¹ If the corporation ratifies the subscription, it ratifies the fraudulent representations of the promoter in obtaining the subscription.²

The Michigan statute requiring representations as to certain facts to be in writing, to be actionable, where false or fraudulent, applies to representations by incorporators as to the credit of the corporation.³

⁹⁵ Greiger v. Salzer, 63 Colo. 167, 165 Pac. 240.

⁹⁶ Lang v. Blocki, 286 Ill. 91, 121 N. E. 163.

⁹⁷ Eastburn v. Grove, 68 Pa. Super. Ct. 363.

⁹⁸ Cator v. Commonwealth Bonding & Casualty Ins. Co., — Tex., 216 S. W. 140.

After bankruptcy of the company a person who had extended credit on the faith of untrue statements in the articles of incorporation, may sue an incorporator who

signed them, for damages. Ver Wys v. Vander Mey, 206 Mich. 499, 173 N. W. 504.

⁹⁹ Bystrom v. Villard, 175 N. Y. App. Div. 433, 162 N. Y. Supp. 100.

¹ Ver Wys v. Vander Mey, 206 Mich. 499, 173 N. W. 504.

² Cator v. Commonwealth Bonding & Casualty Ins. Co., — Tex., 216 S. W. 140.

³ Ver Wys v. Vander Mey, 206 Mich. 499, 173 N. W. 504.

CHAPTER 6

POWER TO CREATE CORPORATIONS

§ 168. Power of state legislature—In general.

§ 171. — Form of incorporating acts.

§ 175. Power of Congress—In general.

§ 168. Power of state legislature—In general. The legislature has power to create, or to provide for creating, corporations to execute trusts, manage trust funds, and act as executors or administrators.¹ The legislature may “prescribe the conditions under which corporations may be organized herein, and may determine the territorial limits of their business operations.”² A corporation cannot complain of a statute in existence at the time of incorporation and the acceptance of which was made a condition of incorporation.³

§ 171. — Form of incorporating acts. A statute entitled “An act to define co-operative associations and to authorize their incorporation” sufficiently expresses its subject in its title although it provides that restrictions on transfers of stock may be made by by-law.⁴

§ 175. Power of Congress—In general.⁵

¹ Attorney General ex rel. Union Trust Co. v. First Nat. Bank of Bay City, 192 Mich. 640, 159 N. W. 335.

² Lukens v. International Life Ins. Co., 269 Mo. 574, 191 S. W. 418.

No one has any vested right in the privilege of organizing a corporation, and hence the legislature may impose such conditions as it deems expedient before allowing it to commence business. *Vale v. Messenger*, 184 Iowa 553, 168 N. W. 281.

³ *International & G. N. Ry. Co. v. Anderson County*, 246 U. S. 424, 62 L. Ed. 807, aff'g — Tex. —, 174 S. W. 305.

⁴ *Chaffee v. Farmers Co-Op. Elevator Co.*, 39 N. D. 585, 168 N. W. 616.

⁵ Article on federal incorporation, see 17 Mich. L. J. 238-260.

Article on nature and extent of power to create federal corporations, see 8 Georgetown L. J. 23-31.

Legal possibilities of federal railroad incorporation, see article in 26 Yale L. J. 207-223.

CHAPTER 7

CREATION UNDER GENERAL LAWS

I. MATTERS TO BE CONSIDERED BEFORE INCORPORATING

§ 180. In general.

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IV. FEES

§ 225. Necessity for payment and amount.

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§ 226. What constitutes.

I. MATTERS TO BE CONSIDERED BEFORE INCORPORATING

§ 180. In general. If the statute provides a particular method for incorporating certain societies, they cannot be incorporated

under the general corporation act.¹ A charter granted under the general law is, in all respects, the equivalent of a charter created by special act of the legislature.²

II. STATUTORY REQUIREMENTS IN GENERAL

§ 181. Preliminary considerations.³ The right to incorporate depends wholly on legislation. Hence if the statute authorizing incorporation is unconstitutional there is no right to incorporate.⁴ If a company attempts to incorporate under a statute relating only to a certain class of corporations, but the powers conferred by the articles were broader than the statute authorized, the corporation, in a proper case, is to be deemed one incorporated under the general statutes.⁵

§ 182. Conditions precedent.⁶ Issuance of certificates of stock is not necessary to the creation of a corporation.⁷ Prior to obtaining a license to do an insurance business, an insurance company has no authority to transact any business and all persons dealing with it are bound to take notice of its limited powers.⁸

Charters to banks are often made dependent upon the consent of a state superintendent of banks or some banking board.⁹

¹ In Pennsylvania, societies operating on the supreme and subordinate lodge plan must be incorporated under the 1893 statute and cannot be incorporated under the general incorporation act. Application of Pennsylvania State Camp, P. O. of A., 261 Pa. 184, 104 Atl. 590.

² In re Hanson's Estate, 38 S. D. 1, 159 N. W. 399.

³ Statutory requirements in South Carolina, see Meyer v. Brunson, 104 S. C. 84, 88 S. E. 359.

⁴ Riddle v. Commissioner of Banking & Insurance, — N. J. L. —, 100 Atl. 692.

⁵ Baldwin County Producers' Corporation v. Frishkorn, — Ala. App. —, 81 So. 862.

⁶ Conditions precedent in Texas, see dicta in Stringfellow v. Pan-

handle Packing Co., — Tex. —, 213 S. W. 250.

In Ohio, the mere filing of the articles of incorporation does not create a corporation. Parkside Cemetery Ass'n v. Cleveland, B. & G. Lake Traction Co., 93 Ohio St. 161, Ann. Cas. 1918 C 1051, 112 N. E. 596.

In Missouri a corporation created under general laws comes into existence when the certificate of incorporation is issued. Williams v. Everett, — Mo. —, 200 S. W. 1045.

⁷ J. W. Williams Co. v. Leong Sue Ah Quin, — Cal. App. —, 186 Pac. 401, and see §§ 5, 12, supra.

⁸ Reynolds v. Union Station Bank of St. Louis, 198 Mo. App. 323, 200 S. W. 711.

⁹ Mulkey v. Bennett, 95 Ore. 70,

§ 186. Conditions subsequent. Failure to complete its road within the specified time does not deprive a railroad company of the title to land purchased.¹⁰ Whether a corporation has violated a statutory provision that it must "proceed to business" within two years after the date of its license cannot be raised collaterally but only by the state in quo warranto proceedings.¹¹

A railroad company whose charter expressly or impliedly requires it to build and operate its whole line, may be required to do so; but if the charter merely authorizes without requiring construction and operation of the road, the company cannot be compelled to complete its road to the point designated as the terminus of the road.¹²

§ 189. Surplusage.¹³

III. INCORPORATION PAPERS

§ 192. In general. In case a certificate of incorporation, by mistake of the attorney preparing it, fails to limit the right to vote to common stockholders, the courts may reform such articles to correspond with the intention of the parties.¹⁴

§ 193. Contents—In general.¹⁵

§ 195. — Purpose of creation and nature of business.¹⁶ The

186 Pac. 1115, and see § 212, *infra*.

In some states, by statute, a bank cannot commence business until a certificate is granted by the state superintendent of banking. *Vale v. Messenger*, 184 Iowa 553, 168 N. W. 281, where scope of discretion of superintendent stated.

¹⁰ *Gulf Lines Connecting R. R. of Illinois v. Golconda Northern Ry.*, 290 Ill. 384, 125 N. E. 357.

¹¹ *La Salle v. Hamilton National Bank*, 204 Ill. App. 518.

¹² *Bentler v. Cincinnati, C. & E. R. Co.*, 180 Ky. 497, L. R. A. 1918 E 315, 203 S. W. 199.

¹³ See § 207, *infra*.

¹⁴ *Millspaugh v. Cassedy*, 191 N. Y. App. Div. 221, 181 N. Y. Supp. 276.

¹⁵ Contents of certificate of incorporation of religious societies as provided for by Pennsylvania statutes, see *Application for Charter of St. Bartholemew's Protestant Episcopal Church*, 260 Pa. 284, 103 Atl. 826.

Statutory form of application for a charter for a water company, presented to public service commission, see *Pennsylvania Power Co. v. Public Service Commission*, 66 Pa. Super. Ct. 448.

¹⁶ See also vol. 1, § 119.

Sufficiency of statement of pur-

purpose for which a corporation is created must be ascertained by referring to the terms of its charter.¹⁷

§ 198. — Limitations on amount of indebtedness.¹⁸ Articles of incorporation do not definitely fix the debt limit where they recite the indebtedness shall not exceed "the amount of two thirds of the shares of stock actually paid up," where the stock paid up is not definitely stated.¹⁹

§ 202. — Statements as to officers and agents. It is sometimes provided in articles of incorporation that, in the absence of actual fraud, contracts or acts of or by a majority of the directors shall not be invalid or voidable because some or all of the directors are interested, and that no director shall be incapacitated from voting by reason of such interest.²⁰

§ 203. — Subscriptions to stock and payment therefor. The articles of incorporation of a water company may provide that stock shall be issued only to the owners of land entitled to water, that the stock shall be transferable only with the land, and that such stockholders shall have the first right to the water.²¹ Where by-laws can be enacted only by the directors, the articles of incorporation cannot provide that no one shall hold more than five shares of stock, the by-laws being silent in regard thereto.²²

pose of corporation for reclaiming wet and overflowed lands, in articles of association, see *Bush v. State*, 187 Ind. 339, 119 N. E. 417.

The reason for requiring this statement is not only to inform the sovereign power but also to create a contract between the incorporators. *Riley v. Callahan Min. Co.*, 28 Idaho 525, 155 Pac. 665.

¹⁷ *Taylor - Critchfield Co. v. Stuckart*, 275 Ill. 129, 113 N. E. 895, and see § 118, *supra*.

¹⁸ Such a provision is primarily for the benefit of the stockholders. *Douglass v. State Bank of Orlando*, — Fla. —, 82 So. 593.

¹⁹ *Parsons v. Rinard Grain Co.*, — Iowa —, 173 N. W. 276.

²⁰ *Whalen v. Hudson Hotel Co.*, 183 N. Y. App. Div. 316, 170 N. Y. Supp. 855, holding, however, that such a provision was without force, as contrary to public policy, if construed as validating a transfer of all the common stock to certain promoters for an option worth much less than the par value of the stock.

²¹ *Riverside Land Co. v. Jarvis*, 174 Cal. 316, 163 Pac. 54.

²² *State ex rel. Daubenspeck v. Day*, — Ind. —, 123 N. E. 402.

§ 204. — **Manner of carrying on business.** The omission of articles of incorporation of a fraternal insurance company to "show the plan of business," as required by the South Dakota statute, is cured by approval of the articles by the commissioner of insurance and the attorney general.²³

§ 207. — **Additional provisions not required by statute.** Unauthorized provisions in the charter are surplusage and do not affect its validity.²⁴

Provisions in an insurance charter, as published, are not notice to a stockholder of facts which the charter is not required by statute to set forth.²⁵ In regard to a life insurance company in Illinois, where the statute sets forth what the proposed charter shall contain, and it was claimed that a subscriber to stock was bound by notice that his money could be used for promotion expenses because of the publication of the charter providing therefor, the supreme court said: "If the publication of a copy of the charter is intended to or does constitute notice, the matters to be stated therein do not include or authorize any provision relating to the acts or authority of the corporations before the corporation would come into being, and the inclusion of such matters could not operate as notice to any one."²⁶

Articles of incorporation of a telephone company, so far as they provide that no one shall own more than five shares of stock, are of no effect, where not required by the statute and

²³ Superior Lodge, Degree of Honor v. Van Camp, 40 S. D. 142, 166 N. W. 545.

²⁴ McIlvaine v. Foreman, 292 Ill. 224, 126 N. E. 749; Holmes Elec. Protective Co. v. Armstrong, 97 N. Y. Misc. 184, 162 N. Y. Supp. 770; Aultz v. Zucht, — Tex. Civ. App. —, 209 S. W. 475.

Unauthorized provisions "are to be treated as surplusage." Holmes Elec. Protective Co. v. Armstrong, 97 N. Y. Misc. 184, 162 N. Y. Supp. 770.

Charter powers which are ultra vires will be treated as surplusage. Ex parte Baldwin County Pro-

ducers' Corporation, — Ala. —, 83 So. 69.

In Indiana, it is held that "as the statute under which appellee was organized does not require that the articles contain such a specification [that 'a board of general managers consisting of three members' shall be appointed], it can have no greater force or effect than as a by-law." Shaw v. Bankers' Nat. Life Ins. Co., — Ind. —, 112 N. E. 16.

²⁵ Lang v. Blocki, 286 Ill. 91, 121 N. E. 163.

²⁶ Lang v. Blocki, 286 Ill. 91, 121 N. E. 163.

where the decision of such questions is vested by statute in the board of directors.²⁷

§ 208. Signatures.²⁸ It is not illegal for an attorney to procure disinterested persons to sign a certificate of incorporation with the understanding that when the charter is granted the subscription is to be assigned to the real owners.²⁹

§ 210. Acknowledgment and verification. Signatures of additional signers of the articles of association need not be acknowledged.³⁰

§ 211. Publication. Where a statute provides that upon filing with the secretary of state proof of publication of the articles of incorporation, "its corporate organization shall be complete," the filing of such proof creates a *de jure* corporation although no capital stock is subscribed or paid for, no books kept, no by-laws adopted, and no meetings held or officers elected.³¹

§ 212. Powers and duties of officer or court. In New York, a proposed membership corporation to further the culture and national aspirations of Catalonia was refused a charter because the declared purposes "if carried out to their ultimate completion might result detrimentally to American interests."³² In Texas, the secretary of state may refuse to issue a charter where he is not satisfied as to the subscription or payment for stock or the value of a patent turned in as part payment for the stock.³³

The discretion of the commissioner of banking, in refusing a charter to a bank, will not be interfered with except in a clear case of abuse of discretion.³⁴ Mandamus does not lie to com-

²⁷ State ex rel. Daubenspeck v. Day, — Ind. —, 123 N. E. 402.

²⁸ In Missouri, the articles must be signed by all of the stockholders at the time of the incorporation. Williams v. Everett, — Mo. —, 200 S. W. 1045.

²⁹ Schmitt v. Kulamer, — Pa. —, 110 Atl. 169.

³⁰ Bush v. State, 187 Ind. 339, 119 N. E. 417.

³¹ Moe v. Harris, — Minn. —, 172 N. W. 494.

³² Application of Catalanian Nationalist Club of New York, 112 N. Y. Misc. 207, 184 N. Y. Supp. 132.

³³ Beach v. McKay, 108 Tex. 224, 191 S. W. 557.

³⁴ State v. Hill, — W. Va. —, 100 S. E. 286.

Duty of banking board to grant

pel the superintendent of banks and trust companies to issue a certificate to a trust company authorizing it to commence business, where there is some basis for a refusal on the ground that the corporation was formed for other purposes, which is a statutory ground for refusal.³⁵

§ 213. Issuance of certificate by officer or court. In Missouri, a corporation comes into existence when the certificate of incorporation is issued.³⁶

§ 215. Filing and recording—General rules.³⁷ The secretary of state will be presumed to have done his duty by filing a certificate of incorporation.³⁸ Recording of the charter is necessary in Pennsylvania as a condition to corporate existence, and until such recordation there is liability of the stockholders for corporate debts as if partners.³⁹

IV. FEES

§ 225. Necessity for payment and amount.⁴⁰ In Illinois the statute requiring payment of fees on filing articles of incorporation, in case of consolidation, was repealed, so far as railroads are concerned, by the provision of the Public Utilities Act requiring payment of a certain per cent on the issuance of stock.⁴¹ For the purpose of paying a fee in Michigan, the

charter to bank as mandatory, see *State ex rel. Woolridge v. Morehead*, 100 Neb. 864, L. R. A. 1917 D 310, 161 N. W. 569.

³⁵ *Farmers' Loan & Trust Bank v. Hirning*, — S. D. —, 172 N. W. 931.

³⁶ *Williams v. Everett*, — Mo. —, 200 S. W. 1045. See also § 182, *supra*.

³⁷ See also § 2949, *infra*.

In Ohio the mere filing of articles of incorporation in due form does not create a corporation. *Parkside Cemetery Ass'n v. Cleveland, B. & G. Lake Traction Co.*, 93 Ohio St. 161, Ann. Cas. 1918 C 1051, 112 N. E. 596.

³⁸ *People v. National Security Co.*, 189 N. Y. App. Div. 38, 177 N. Y. Supp. 838.

³⁹ *Campbell v. Beaman*, 68 Pa. Super. Ct. 30.

⁴⁰ A packing company was held a "co-operative" corporation within the North Dakota statutes as to fees for filing amended articles of incorporation in case of co-operative corporations, in *Equity Co-operative Packing Co. v. Hall*, — N. D. —, 173 N. W. 796.

⁴¹ *New York Cent. R. Co. v. Stevenson*, 277 Ill. 474, 115 N. E. 633.

no par value stock of a Delaware corporation must be taken at the par value of \$100 as required by the Delaware statutes.⁴²

Filing amended articles of incorporation whereby the capital stock was more than doubled, the corporate life extended over 75 years, and the name changed, does not create a new corporation so far as the duty, in Kentucky, to pay an organization tax is concerned.⁴³ Amending the articles of incorporation by increasing the amount of capital stock is not an "increase of its powers" within the Kentucky statute so as to make it liable for an organization tax on the original stock as well as on the increase.⁴⁴

Building and loan associations cannot escape payment of fees on filing an amendment increasing the amount of their capital stock, as provided for by statute relating to corporations generally, on the theory that they have no regular capital stock or that such stock is an uncertain or varying amount.⁴⁵

V. CHARTER

§ 226. What constitutes. The charter of a company consists of its articles of incorporation and the general statutes under which the organization takes place.⁴⁶

⁴² *Detroit Mortg. Corporation v. Vaughan*, 211 Mich. 320, 178 N. W. 697.

On amending its charter changing common stock of \$10 par value to no par value, a Delaware corporation must pay, in Michigan, a franchise fee on the stock computing it at the par value of \$100 a share as required by the Delaware statutes. *Detroit Mortg. Corporation v. Vaughan*, 211 Mich. 320, 178 N. W. 697.

⁴³ *Com. v. Belknap Hardware & Manufacturing Co.*, 182 Ky. 155, 206 S. W. 277, overruling earlier Kentucky cases so far as they hold a contrary rule. See also *Louisville Gas & Electric Co. v. Bosworth*, 169 Ky. 824, 185 S. W. 125.

⁴⁴ *Greene v. Louisville R. Co.*, 184 Ky. 91, 211 S. W. 418.

⁴⁵ *State ex rel. Equitable Building, Loan & Savings Ass'n v. Amsherry*, — Neb. —, 178 N. W. 828.

⁴⁶ *Wegener v. Wegener*, — Ohio St. —, 126 N. E. 892.

The charter consists of the articles of incorporation "and the laws of the state under which such corporation has been created." *In re Hanson's Estate*, 38 S. D. 1, 159 N. W. 399.

Powers and privileges contained in articles of incorporation, permissible under the statutes, are a part of the charter. *In re Hanson's Estate*, 38 S. D. 1, 159 N. W. 399.

CHAPTER 8

CREATION UNDER SPECIAL ACTS

§ 228. Constitutional prohibitions against special acts.

§ 231. Corporations within prohibition.

§ 233. What constitutes creation of corporation.

§ 236. What constitutes granting or conferring of corporate powers or privileges.

§ 239. Acceptance of charter—Necessity.

§ 243. — Time.

§ 245. — Formal acceptance.

§ 228. Constitutional prohibitions against special acts.¹ Where there is an existing general law for the incorporation of railway companies, it is a violation of the state constitution to enact a special law relating thereto.² The power to organize as a corporation under a special statute is terminated by the adoption of a constitutional provision forbidding such corporations.³

A bank illegally organized under a special act cannot claim vitality because of general statutes under which it might thereafter have been created.⁴

§ 231. Corporations within prohibition.⁵

¹History of Missouri legislation, see *State ex rel. Kinloch Tel. Co. v. Roach*, 269 Mo. 437, 190 S. W. 862.

Pennsylvania provision, see *Germantown Trust Co. v. Powell*, 265 Pa. 71, 108 Atl. 441.

²*Morrison v. Cook*, 146 Ga. 570, 91 S. E. 671.

³*Davis v. Allison*, 109 Tex. 440, 211 S. W. 980.

⁴*Davis v. Allison*, 109 Tex. 440, 211 S. W. 980.

⁵An insurance association cre-

ated by a Workmen's Compensation Act was held in Texas not a private corporation within the constitution prohibiting creation of private corporations by special act. *Middleton v. Texas Power & Light Co.*, 108 Tex. 96, 11 N. C. C. A. 873, 185 S. W. 556.

Under the Constitution of South Dakota, religious corporations cannot be created by special act. *In re Hanson's Estate*, 38 S. D. 1, 159 N. W. 399.

§ 233. **What constitutes creation of corporation.** The statute itself need not call its creation a "corporation" in order to make it one.⁶

§ 236. **What constitutes granting or conferring of corporate powers or privileges.**⁷

§ 239. **Acceptance of charter.—Necessity.** Acceptance is necessary, to create a contract, of a special statute authorizing incorporation.⁸

§ 243. — **Time.** The acceptance must be within a reasonable time. A corporation which has not organized so as to accept the charter cannot organize after the enactment of a constitutional provision prohibiting such corporations.⁹

§ 245. — **Formal acceptance.** The "acceptance must be effected by organization of the corporation, and where no time is fixed by the act, it must be within a reasonable time."¹⁰

⁶ In re Carthage Lodge No. 365, I. O. O. F., 230 Fed. 694.

⁷ What is grant of "corporate powers" as to which special or private laws are forbidden, see Outagamie County v. Zuehlke, 165 Wis. 32, 161 N. W. 6.

⁸ Davis v. Allison, — Tex. Civ. App. —, 189 S. W. 968.

⁹ Davis v. Allison, 109 Tex. 440, 211 S. W. 980.

¹⁰ Davis v. Allison, 109 Tex. 440, 211 S. W. 980.

CHAPTER 9

ORGANIZATION

§ 250. Terminology.

§ 251. Elements.

§ 252. Necessity of organization.

§ 253. Time for organization—In the absence of statute.

§ 254. — Under constitutional and statutory provisions.

§ 257. Procedure generally to effect organization.

§ 271. Report of commissioners, corporators or officers.

§ 250. Terminology.¹

§ 251. Elements.²

§ 252. Necessity of organization.³ Until a corporation is organized, it cannot transfer title to a note payable to the corporation.⁴ Where a statute provides that "it shall not be lawful for such companies" to "transact any business" before organization and subscription to all the corporate stock, a contract made by the incorporators before such organization is not merely voidable but is void and cannot be ratified.⁵ In Colorado, the organization of insurance companies, including the designation of certain incorporators to receive stock subscriptions, is specially regulated by statute.⁶

¹ Organization defined, see Com. v. John McGlinn Distilling Co., 265 Pa. 346, 108 Atl. 823.

"Organized" is often used synonymously with "incorporated." Superior Lodge, Degree of Honor v. Van Camp, 40 S. D. 142, 166 N. W. 545.

² In Minnesota, by statute, "corporate organization shall be complete" on the filing of proof of publication of articles of incorporation. Moe v. Harris, — Minn. —, 172 N. W. 494.

³ That company must be or-

ganized in Ohio before it can exercise the power of eminent domain, see Parkside Cemetery Ass'n v. Cleveland, B. & G. Lake Traction Co., 93 Ohio St. 161, Ann. Cas. 1918 C 1051, 112 N. E. 596.

⁴ Frankel v. Ashmore, 208 Ill. App. 410.

⁵ Missouri Fidelity & Casualty Co. v. Scott & Scott, — Okla. —, 178 Pac. 122, construing Missouri statute.

⁶ Greiger v. Salzer, 63 Colo. 167, 165 Pac. 240.

§ 253. Time for organization—In the absence of statute. Organization, as an acceptance of a charter granted by a special act, must be within a reasonable time.⁷

§ 254. — Under constitutional and statutory provisions. A constitutional provision requiring organization of corporations and commencement of business within 2 years from the date of the charter or grant of corporate franchise is not violated by failure to file a report of the organization with the secretary of state within 30 days, as required by statute, since the report is not a step necessary to perfect the organization.⁸

§ 257. Procedure generally to effect organization.⁹ The new corporation act of Illinois abolishes commissioners to take subscriptions.¹⁰

§ 271. Report of commissioners, corporators or officers. A statutory requirement that a corporation file its report of organization with the secretary of state within 30 days after organization may be dispensed with by statute passed after the corporation has failed to meet the requirement. The court said: "In other words, a formality to be observed either in the organization of a corporation or by it after its organization, which the legislature could have dispensed with in advance, may be dispensed with by the legislature after the time for the observance of it has passed."¹¹ In Illinois the report, if any part of the capital has been paid in in property, must state the fair cash value thereof.¹²

⁷ Davis v. Allison, 109 Tex. 440, 211 S. W. 982.

⁸ Southern Coal Co. v. Yazoo Ice & Coal Co., 118 Miss. 860, 80 So. 334.

⁹ Procedure in South Carolina, see Meyer v. Brunson, 104 S. C. 84, 88 S. E. 359.

¹⁰ See article in 14 Ill. L. Rev.

356-377 by Mr. William Brown Hale on "The New Corporation Act and the Securities Law."

¹¹ Southern Coal Co. v. Yazoo Ice & Coal Co., 118 Miss. 860, 80 So. 334.

¹² Central Trust Co. v. Crawford, 201 Ill. App. 555.

CHAPTER 10

DE FACTO CORPORATIONS

I. GENERAL CONSIDERATIONS

§ 273. Definition and nature.

II. DOCTRINE IN RELATION TO COLLATERAL ATTACK

§ 274. Statement of the rule.

§ 275. Statutory provisions.

§ 276. Basis of and reasons for the rule.

§ 277. Limitations of and exceptions to rule.

III. REQUISITES OF CORPORATIONS DE FACTO

§ 278. General statement.

§ 279. Lawful authority for existence of corporation—In general.

§ 281. —Corporations prohibited by statute or contrary to public policy.

§ 285. —Expiration or forfeiture of charter.

§ 289. Bona fide attempt to incorporate.

§ 290. Compliance with provisions of statute or charter—In general

§ 294. —Execution of articles or certificate.

§ 297. —Provisions as to capital stock.

§ 298. —Filing or recording articles or certificate.

§ 301. —Provisions as to organization.

§ 302. —Consolidation, reorganization and amendment.

IV. RIGHTS AND LIABILITIES OF DE FACTO CORPORATIONS AND THEIR MEMBERS

§ 305. Contracts with de facto corporations.

§ 306. Ownership of property and conveyances of same.

§ 315. Torts by and against—Torts against.

§ 321. Rights and liabilities of members and officers—Statutory liability for corporate debts.

I. GENERAL CONSIDERATIONS

§ 273. Definition and nature.¹

1 Missouri cases relating to de Extension of the doctrine of de
facto corporations, see article in facto corporations, see article in
3 St. Louis L. Rev. 175-204. 19 Columbia L. Rev. 391-395.

II. DOCTRINE IN RELATION TO COLLATERAL ATTACK

§ 274. Statement of the rule. A corporation de facto cannot be collaterally attacked² as to the regularity of its incorporation.³ Corporate existence cannot be attacked by a private individual.⁴ This rule that only the state can attack a de facto corporation applies equally well to a de facto consolidated corporation.⁵

§ 275. Statutory provisions. In California a statute prohibits collateral attack on the existence of a de facto corporation.⁶ Such a statute does not apply to corporations expressly forbidden by law,⁷ nor preclude a private person from denying the existence de jure or de facto of an alleged corporation.⁸

§ 276. Basis of and reasons for the rule. The de facto rule precluding collateral attack does not rest merely on estoppel but on public policy, and there need be no estoppel.⁹

§ 277. Limitations of and exceptions to rule. A de facto consolidated corporation may be attacked by a minority stockholder for fraud practiced by the directors on the stockholders without violating the general rule as to collateral attack.¹⁰

² Root v. Wear, 98 Kan. 234, 157 Pac. 1181; Alder Slope Ditch Co. v. Moonshine Ditch Co., 90 Ore. 385, 176 Pac. 593. See also Carolina-Tennessee Power Co. v. Hiawassee River Power Co., 175 N. C. 668, 676, 96 S. E. 99.

In Pennsylvania, in a proceeding brought under P. L. 1360 (Act June 19, 1871) to restrain a public service company from violating its charter, an individual cannot attack collaterally the corporate franchise or charter. Curry v. Harmony Elec. Co., 251 Pa. 344, 96 Atl. 822.

³ Alder Slope Ditch Co. v. Moonshine Ditch Co., 90 Ore. 385, 176 Pac. 593.

⁴ Root v. Wear, 98 Kan. 234, 236, 157 Pac. 1181.

⁵ Alabama Fidelity Mortgage & Bond Co. v. Dubberly, 198 Ala. 545, 73 So. 911.

⁶ McCann v. Children's Home Society, 176 Cal. 359, 168 Pac. 355.

⁷ Davis v. Allison, — Tex. Civ. App. —, 189 S. W. 968.

⁸ Crow v. Cattlemen's Trust Co., — Tex. Civ. App. —, 198 S. W. 1047.

⁹ Kardo Co. v. Adams, 231 Fed. 950, 968.

¹⁰ Alabama Fidelity Mortgage & Bond Co. v. Dubberly, 198 Ala. 545, 73 So. 911.

III. REQUISITES OF CORPORATIONS DE FACTO

§ 278. General statement.¹¹ To constitute a corporation de facto "three things are necessary: (1) Some law under which a corporation with powers assumed may lawfully have been created; (2) a colorable and bona fide attempt to perfect an organization under such a law; and (3) user of the rights claimed to have been conferred by the law—that is, of the corporate franchise."¹² A corporation, although not a de jure one for lack of a charter issued by the secretary of state, is, at least in Missouri, a de facto one where there was a statute permitting it to be organized, user of the powers assumed, and the taking of part of the necessary steps to organize as a corporation.¹³ Where a corporation could be lawfully created, and a bona fide and colorable attempt is made to do so, a de facto corporation may result, however irregular, informal or defective the incorporation proceedings may be.¹⁴

§ 279. Lawful authority for existence of corporation—In general. There can be no de facto corporation unless there is a law authorizing such a corporation.¹⁵

¹¹ Irrigation district as de facto corporation, see *Fisher v. Pioneer Const. Co.*, 62 Colo. 538, 163 Pac. 851.

An able and exhaustive decision by Judge Hollister relating to what constitutes a de facto corporation in Ohio, reviewing the Ohio decisions at length, is found in *Kardo Co. v. Adams*, 231 Fed. 950, rev'g *American Ball Bearing Co. v. Adams*, 222 Fed. 967.

¹² *Nelson v. Consolidated Independent School Dist. of Troy Mills*, 181 Iowa 424, 164 N. W. 874; *Pocahontas Fuel Co. v. Tarboro Cotton Factory*, 174 N. C. 245, 93 S. E. 790; *Alder Slope Ditch Co. v. Moonshine Ditch Co.*, 90 Ore. 385, 176 Pac. 593. See also *W. A. Case & Son Mfg. Co. v. Norman*, 211 Ill. App. 311.

There is a de facto corporation, at least in Oregon, where there is (1) a law under which the corporation could be organized, (2) a bona fide attempt to organize a corporation, and (3) an actual use of corporate powers. *Alder Slope Ditch Co. v. Moonshine Ditch Co.*, 90 Ore. 385, 176 Pac. 593.

¹³ *Meramee Spring Park Co. v. Gibson*, 268 Mo. 394, 402, 188 S. W. 179.

¹⁴ *Alabama Fidelity Mortgage & Bond Co. v. Dubberly*, 198 Ala. 545, 73 So. 911.

¹⁵ *People ex rel. Robinson v. New York Cent. R. Co.*, 283 Ill. 334, 119 N. E. 299; *Crow v. Cattlemen's Trust Co.*, — Tex. Civ. App. —, 198 S. W. 1047.

§ 281. — Corporations prohibited by statute or contrary to public policy.¹⁶

§ 285. — Expiration or forfeiture of charter. After the expiration of its corporate life, a corporation continuing to act as such is sometimes considered a de facto corporation.¹⁷ If a statute limits the corporate life, it is said in Arkansas, there is no de facto corporation after the charter has expired, but if the articles of incorporation limit the corporate existence there may be a de facto corporation after the charter has expired.¹⁸ In the Supreme Court of New York, it was held, following a West Virginia decision, that a corporation which continued business after the term of its existence, without any proceeding to wind it up, was a de facto corporation.¹⁹ In Missouri, a de facto corporation, the same as a de jure one, ceases to exist after the term fixed by law as the period of its existence has expired.²⁰

§ 289. Bona fide attempt to incorporate. There can be no de facto corporation unless there is an effort to organize under the law authorizing the corporation.²¹ Good faith is a "vital fact."²²

§ 290. Compliance with provisions of statute or charter—In general. Where the three corporations promoting the formation of another corporation had power to do so, the purpose of incorporation was legitimate, the articles of incorporation were properly filed, ten per cent of the capital stock was subscribed and one-tenth paid in, the company acted as a corporation and had a seal and was equipped to carry on business, and no wrong was perpetrated or sought to be perpetrated, there is a corporation de

¹⁶ General rule restated in *Davis v. Allison*, — Tex. Civ. App. —, 189 S. W. 968.

¹⁷ *Wilson v. Brown*, 107 N. Y. Misc. 167, 175 N. Y. Supp. 688.

¹⁸ *Arlington Hotel Co. v. Rector*, 124 Ark. 90, 186 S. W. 622.

¹⁹ *Wilson v. Brown*, 107 N. Y. Misc. 167, 175 N. Y. Supp. 688.

²⁰ *Meramec Spring Park Co. v. Gibson*, 268 Mo. 394, 406, 188 S. W. 179, where the court said a

contrary rule would mean "observe the law, become a de jure corporation and die of old age in twenty years; refuse to follow the law, become a de facto corporation and live forever."

²¹ *People ex rel. Robinson v. New York Cent. R. Co.*, 283 Ill. 334, 119 N. E. 299.

²² *Kardo Co. v. Adams*, 231 Fed. 950, 966.

facto, under the laws of Ohio, although the statutory provisions as to issuance of stock and election of directors have not been lawfully complied with.²³ A corporation is not precluded from being a de facto one because the subscriptions of the five agents, who were the incorporators, although paid to the corporation, were merely as dummies in behalf of separate corporations, and because the subsequent election of directors by such agents was not an election by the real stockholders.²⁴

§ 294. — Execution of articles or certificate. Failure to verify the articles of incorporation does not preclude the existence of a de facto corporation.²⁵

§ 297. — Provisions as to capital stock.²⁶

§ 298. — Filing or recording articles or certificate. If the charter is not filed in the county where the principal office is located, as required by statute, stockholders are liable as partners, because in such a case there is not even a de facto corporation, it is held in Illinois.²⁷ In Arkansas, filing the articles of association with the county clerk but not with the secretary of state, followed by the doing of business as a corporation, creates a de facto corporation.²⁸ In Oregon, it seems that where the law authorizes the creation of a corporation, there is a good faith attempt to incorporate, and the corporation proceeds to exercise corporate functions as a corporation, there is a corporation de facto though the articles of incorporation were not properly filed.²⁹ In Tennessee, failure to record the certificate in the county where its principal office is located, as required by the statutes relating to religious corporations, prevents even a de facto corporation.³⁰

²³ *Kardo Co. v. Adams*, 231 Fed. 950, 967, rev'g *American Ball Bearing Co. v. Adams*, 222 Fed. 967.

²⁴ *Kardo Co. v. Adams*, 231 Fed. 950, 965, rev'g *American Ball Bearing Co. v. Adams*, 222 Fed. 967.

²⁵ *McCann v. Children's Home Society*, 176 Cal. 359, 168 Pac. 355.

²⁶ See § 290, *supra*.

²⁷ *Hall v. Robertson*, 213 Ill. App. 147.

²⁸ *Wesco Supply Co. v. Smith*, 134 Ark. 23, 203 S. W. 6.

²⁹ *Grant Chrome Co. v. Marks*, 92 Ore. 443, 181 Pac. 345, citing *Fletcher's Cyc. Corp.* § 278.

³⁰ *Hunter v. Swadley*, 141 Tenn. 156, 207 S. W. 730.

§ 301. — **Provisions as to organization.**³¹ In considering the South Carolina statute providing that mere “irregularities” shall not affect the creation of a corporation, the court said: “We take it that the legislature meant that a failure of the incorporators to comply regularly and exactly with all the provisions of the law about the formation of corporations should not vitiate the charter. We think that it did not mean that the incorporators might ignore the substance of the law and escape.” In that case a petition for a commission to issue to organize a corporation was followed by the opening of books of subscription and a quarter of the stock was subscribed; but only a part was paid for and no meeting was held or certificate secured or return made as required by statute, and the court held the incorporators liable individually on the theory that there was not even a de facto corporation.³²

§ 302. — **Consolidation, reorganization and amendment.** There is a de facto consolidated corporation where, although the procedure to consolidate is irregular and invalid, every necessary step taken was within the powers of the constituent companies and there was a merger agreement ratified by the stockholders and an amendment of the charter.³³

IV. RIGHTS AND LIABILITIES OF DE FACTO CORPORATIONS AND THEIR MEMBERS

§ 305. **Contracts with de facto corporations.** There is no essential difference between a de jure and a de facto corporation as to individuals who have dealt with it as a corporation.³⁴

§ 306. **Ownership of property and conveyances of same.** Conveyances of land by a corporation are binding as against everybody but the state without regard to whether the corporation is

³¹ There may be a corporation de facto although no capital stock is subscribed or paid for, no by-laws adopted, no books kept, and no meetings held or officers elected. *Moe v. Harris*, — Minn. —, 172 N. W. 494.

³² *Meyer v. Brunson*, 104 S. C. 84, 88 S. E. 359.

³³ *Alabama Fidelity Mortgage & Bond Co. v. Dubberly*, 198 Ala. 545, 73 So. 911.

³⁴ *Pocahontas Fuel Co. v. Tarboro Cotton Factory*, 174 N. C. 245, 93 S. E. 790.

a de jure or de facto one.³⁵ The assignment of a patent to a de facto corporation is valid and binding against all the world except the state.³⁶

§ 315. Torts by and against—Torts against. A wrongdoer cannot deny the capacity of a de facto corporation suing him to redress the wrong.³⁷

§ 321. Rights and liabilities of members and officers—Statutory liability for corporate debts. Stockholders are liable for corporate debts, where liability is imposed by statute, regardless of the fact that the corporation is merely a de facto one.³⁸

³⁵ Cotton v. White, 131 Ark. 273, 199 S. W. 116.

³⁶ Kardo Co. v. Adams, 231 Fed. 950, 971.

³⁷ Kardo Co. v. Adams, 231 Fed. 950, 970.

³⁸ Wesco Supply Co. v. Smith, 134 Ark. 23, 203 S. W. 6.

CHAPTER 11

CORPORATIONS BY ESTOPPEL

II. ESSENTIAL REQUISITES OF ESTOPPEL

§ 325. Good faith, knowledge, notice and reliance.

§ 326. Necessity for de facto corporate existence.

III. ACTS CONSTITUTING ESTOPPEL AND PERSONS ESTOPPED

§ 334. Estoppel of persons contracting or dealing with corporation—In general.

§ 336. — Contracting in name implying corporate existence.

§ 337. — Conveyances, mortgages and leases.

§ 338. — Bonds.

§ 342. — Limitations upon and exceptions to the rule.

§ 343. Estoppel of pretended corporation—In general.

§ 345. — Use of name importing corporate existence.

§ 346. — Applications of the rule.

§ 348. Estoppel of promoters, members and officers of pretended corporation—Estoppel of promoters and members.

§ 349. — Estoppel of officers.

§ 350. — Estoppel of members and officers as between themselves or as against the corporation.

§ 352. Estoppel arising from actions by or against pretended corporation—Estoppel of persons suing or sued by corporation.

§ 354. — Estoppel of corporation.

II. ESSENTIAL REQUISITES OF ESTOPPEL

§ 325. **Good faith, knowledge, notice and reliance.** There is no estoppel where the other party has not been misled or deceived as to the capacity in which the association made its contracts with him.¹

§ 326. **Necessity for de facto corporate existence.** In Missouri it has recently been held that the estoppel rule “does not

¹ *Simpson v. Grand International Engineers*, 83 W. Va. 355, 98 S. E. 580.

extend to a case where no charter has been obtained from the secretary of state and there has never been an intention to obtain such a charter.''² However, estoppel of persons dealing with a corporation as such, to deny corporate existence, applies to persons dealing with de facto corporations.³

III. ACTS CONSTITUTING ESTOPPEL AND PERSONS ESTOPPED

§ 334. Estoppel of persons contracting or dealing with corporation—In general. All who deal with a corporation as such are estopped to deny its corporate existence.⁴ Correspondence by a party dealing with a corporation, in its corporate name, estops one to dispute liability on the ground that the corporation was not even a de facto one.⁵ If one deals with another as a corporation, he should not be permitted to hold the other liable individually as a partner.⁶ Where two parties contract and deal with each other as corporations, each is estopped to deny the corporate existence of the other.⁷

§ 336. — Contracting in name implying corporate existence. According to some of the decisions, there is a difference between contracting with another as a certain "company" and as a certain "corporation," on the theory that the word "company" is equally applicable to a partnership.⁸ It is held in Kansas that "one who has signed a promissory note running to a payee described by a name appropriate to a corporation, although not employing that term, cannot, in an action brought against him thereon by such payee under the same name, in which it

² Talbert v. Grist, 198 Mo. App. 492, 496, 201 S. W. 906.

³ Wesco Supply Co. v. Smith, 134 Ark. 23, 203 S. W. 6.

⁴ Dorris v. Farmers' & Merchants' Bank, 22 Ga. App. 514, 96 S. E. 450; Faulkner v. Farmers' Produce & Mercantile Co., 170 Ky. 22, 185 S. W. 151.

A person who contracts with a corporation and transacts business with it in that capacity is estopped to deny its corporate existence in an action involving an alleged breach of the contract. Farmers'

League & Community Tel. Ass'n v. Ohio & M. Val. Tel. Co., 194 Ill. App. 166.

⁵ W. A. Case & Son Mfg. Co. v. Norman, 211 Ill. App. 311, and see § 326.

⁶ Wesco Supply Co. v. Smith, 134 Ark. 23, 203 S. W. 6.

⁷ Northwest Auto Co. v. Harmon, 250 Fed. 832, 837.

⁸ Lowell-Woodward Hardware Co. v. Woods, 104 Kan. 729, 180 Pac. 734, reviewing decisions pro and con.

alleges itself to be a corporation, be heard to question the plaintiff's corporate existence, unless upon a showing that his obligation to make payment would be thereby affected."⁹ "What names import corporation within rule that one contracting with body described by corporate name is estopped to deny its corporate existence" is the title of a recent extensive note.¹⁰

§ 337. — Conveyances, mortgages and leases. A mortgagor who has dealt with the mortgagee as a corporation, and received from it the consideration of the mortgage note, is estopped from denying its corporate capacity in an action by the corporation to foreclose the mortgage.¹¹ A deed, by describing the grantee as a corporation duly organized, estops the grantor to deny corporate existence of the grantee.¹² A deed executed to a company before its incorporation is nevertheless valid.¹³

§ 338. — Bonds. Executing an attachment bond reciting defendant's name as "Barnum & Bailey's Circus, a corporation" estops defendant to deny its incorporation.¹⁴

§ 342. — Limitations upon and exceptions to the rule. An unauthorized contract not executed by the corporation or by any one authorized to act for it cannot operate as an estoppel against the other party to deny corporate existence.¹⁵ Where a person extends credit to an alleged corporation and sues to recover the debt, no estoppel arises against him because he has dealt with the defendant as a corporation. The estoppel arises ordinarily only where one is seeking to resist recovery.¹⁶

⁹ Lowell - Woodward Hardware Co. v. Woods, 104 Kan. 729, 180 Pac. 734.

¹⁰ 5 A. L. R. 1580, annotating Ingle System Co. v. Norris & Hall, 132 Tenn. 472, 5 A. L. R. 1578, 178 S. W. 1113.

¹¹ J. I. Case Threshing Mach. Co. v. Copren Bros., — Cal. App. —, 187 Pac. 772.

¹² McCann v. Children's Home Society, 176 Cal. 359, 168 Pac. 355.

¹³ Beggs v. Myton Canal & Irrigation Co., — Utah —, 179 Pac. 984.

¹⁴ Burke v. Barnum & Bailey, 40 R. I. 71, 99 Atl. 1027.

¹⁵ Mechanicville & Ft. E. R. Co. v. Fitchburg R. Co., 103 N. Y. Misc. 46, 170 N. Y. Supp. 476.

¹⁶ Incorporation by estoppel can be urged "very rarely, if ever," where "the claimant, having extended credit or value towards the alleged corporation, is seeking to recover its debt." Pocahontas Fuel Co. v. Tarboro Cotton Factory, 174 N. C. 245, 93 S. E. 790.

Where a corporation is organized in one state with a fixed purpose not to transact any business in that state, it is held in Texas that such conduct is a fraud upon the state granting the charter, and a person dealing with the alleged corporation in another state is not thereby estopped to deny its corporate existence in order to hold its directors personally liable as partners.¹⁷

§ 343. Estoppel of pretended corporation—In general. Both the corporation, its stockholders, and persons in privity, are estopped to attack the validity of the statute under which the company was incorporated,—the statute being a part of the charter.¹⁸ A foreign corporation which has not completed its organization in its home state, but which is doing business as a corporation in another state, is estopped to deny its corporate existence to invalidate service of process on it through an agent.¹⁹

§ 345. — Use of name importing corporate existence. A labor union, which is a voluntary association consisting of local unions throughout the United States, is estopped to deny its corporate existence where it bears a name implying a corporation and is organized the same as a corporation.²⁰

§ 346. — Applications of the rule. A corporation which has ratified a purchase for it, and also the mortgage executed for the price, is estopped to deny the validity of the mortgage on the ground that the charter of the company had not been filed when the mortgage was executed.²¹

§ 348. Estoppel of promoters, members and officers of pretended corporation—Estoppel of promoters and members. A

¹⁷ Scharbauer v. Lampass County, — Tex. Civ. App. —, 214 S. W. 468.

¹⁸ Winthrop v. Fellows, 230 Fed. 702.

¹⁹ Charles Ehrlich & Co. v. J. Ellis Slater Co., — Cal. —, 192 Pac. 526.

²⁰ Dugan v. International Ass'n of Bridge & Structural Iron Workers, 202 Ill. App. 308.

²¹ A corporation is estopped to deny the validity of a purchase price mortgage executed prior to its creation as a corporation where it has accepted and used the mortgaged property. Thorndale Mercantile Co. v. Continental Gin Co., — Tex. Civ. App. —, 217 S. W. 1059.

stockholder sued by a receiver cannot attack the validity of the incorporation of the company.²² Subscribers to stock are estopped to plead nonexistence of the corporation when sued by a receiver of the company—a de facto corporation—to recover assessments on the stock for the benefit of creditors.²³

§ 349. — Estoppel of officers. One who participated in the organization of a corporation, served as director, and has received dividends, cannot urge that the corporation is a fiction.²⁴

§ 350. — Estoppel of members and officers as between themselves or as against the corporation.²⁵

§ 352. Estoppel arising from actions by or against pretended corporation—Estoppel of persons suing or sued by corporation. One suing a corporation as such is estopped, in a subsequent suit, to deny its corporate existence, at least under ordinary circumstances.²⁶ Whether making a so-called corporation a defendant amounts to an admission of its corporate existence depends upon the allegations of the complaint, since the mere inclusion of a name as a defendant does not operate as an admission against an express averment in the complaint to the contrary.²⁷ Making a so-called corporation a defendant will not amount to an admission of its corporate existence where the complaint alleges it is not a corporation.²⁸

§ 354. — Estoppel of corporation. Defendant cannot deny its corporate character after appearing and pleading as such.²⁹ But taking of an appeal from a justice by a defendant does not

²² Weitzel v. Brown, 224 Mass. 190, 112 N. E. 945.

²³ Allen v. Rhodes, 230 Fed. 321.

²⁴ Baillie v. Columbia Gold Min. Co., 86 Ore. 1, 167 Pac. 1167.

²⁵ See § 348, supra.

²⁶ Stearns Coal & Lumber Co. v. Jamestown R. Co., 141 Tenn. 203, 208 S. W. 334.

²⁷ Nelson v. Consolidated Independent School Dist. of Troy Mills, 181 Iowa 424, 164 N. W. 874.

²⁸ Nelson v. Consolidated Independent School Dist. of Troy Mills, 181 Iowa 424, 164 N. W. 874.

²⁹ Burke v. Barnum & Bailey, 40 R. I. 71, 99 Atl. 1027.

But a mere appearance, at least in a justice court, does not preclude a subsequent plea denying corporate existence of defendant. Mitch v. United Mine Workers, — W. Va. —, 104 S. E. 292.

waive proof of its corporate existence, where otherwise necessary.³⁰

³⁰ Appearance of defendant for the purpose of taking an appeal from a justice court does not bar the right to plead want of corporate existence of defendant on appeal. *Mitch v. United Mine Workers*, — W. Va. —, 104 S. E. 292.

CHAPTER 12

INCORPORATION OF PARTNERSHIPS, ASSOCIATIONS AND TENANTS IN COMMON

- § 359. Agreement of members to incorporate.
- § 361. Name of corporation.
- § 362. Effect of formation of corporation on existence of partnership or association.
- § 363. Notice of change from partnership to corporation.
- § 373. Conveyance of firm or association property to corporation—Fraud and fraudulent conveyances.
- § 374. Rights of corporation as to contracts of and debts due to partnership or association.
- § 375. Liability of corporation on debts or contracts of partnership or association—In general.
- § 377. — Assumption either express or implied.
- § 384. Liability of partners or members on contracts and for debts.
- § 386. Incorporation of tenants in common.

§ 359. Agreement of members to incorporate. Contracts of partners to dissolve and form a corporation are valid.¹ Partners cannot have the benefit of an agreement to incorporate and evade the provisions thereof by which their respective rights in the partnership assets are determined.²

§ 361. Name of corporation. The sale by a partnership to a corporation of the business and good will of the firm carries with it the right to continue the business in the partnership name.³

§ 362. Effect of formation of corporation on existence of partnership or association. A partnership is terminated and merged where the partners incorporate the business, unless otherwise agreed.⁴

¹ Nannizzi v. Caprile, — Cal. v. Review Pub. Co., 139 Minn. App. —, 185 Pac. 673. 358, L. R. A. 1918 D 154, 166 N.

² Nannizzi v. Caprile, — Cal. W. 413.
App. —, 185 Pac. 673.

⁴ Cavasso v. Downey, — Cal.

³ Twin City Brief Printing Co. App. —, 188 Pac. 594.

§ 363. Notice of change from partnership to corporation.⁵

Where a partnership becomes incorporated without knowledge of one dealing with the firm, settlement with the partners is a settlement with the corporation.⁶

§ 373. Conveyance of firm or association property to corporation—Fraud and fraudulent conveyances. Transfers of personal property by a partnership to a corporation as its successor, without change of possession, are fraudulent as to a creditor of the firm not notified of the change.⁷

§ 374. Rights of corporation as to contracts of and debts due to partnership or association.⁸ A guaranty of the account of a customer of a partnership does not survive the dissolution of the partnership, in favor of a corporation as successor of the firm.⁹

§ 375. Liability of corporation on debts or contracts of partnership or association—In general. A corporation which is a successor of a partnership and takes over the firm business is bound by an estoppel created by a contract made by the firm.¹⁰

§ 377. — Assumption either express or implied. A corporation which is the successor of a partnership adopts a contract of the firm by affirmative acts relating thereto with knowledge thereof.¹¹

§ 384. Liability of partners or members on contracts and for debts. An attempt to collect a claim against a corporation in

⁵ Notice of incorporation of partnership, see *Ivy v. Binswanger & Co.*, 141 Tenn. 568, 214 S. W. 74.

⁶ *White v. Kincaid*, — Cal. —, 179 Pac. 685.

⁷ *White v. Kincaid*, — Cal. —, 179 Pac. 685.

⁸ Liability of corporation as successor of partnership, see *McPike v. Kardell Motorecar Co.*, — Mo. App. —, 213 S. W. 904.

Contracts of partnership as

binding on its successor, a corporation, see *Interstate Finance Corporation v. Commercial Jewelry Co.*, 280 Ill. 116, 117 N. E. 440, aff'g 201 Ill. App. 568.

⁹ *John Wanamaker v. Shoemaker*, 70 Pa. Super. Ct. 473.

¹⁰ *Dudlo Mfg. Co. v. Varley Duplex Magnet Co.*, 253 Fed. 745.

¹¹ *J. L. Mott Iron Works v. Kaiser Co.*, — S. C. —, 103 S. E. 783.

the hands of a receiver does not preclude the right to collect it from partners, where the corporation was a successor of the partnership.¹²

§ 386. Incorporation of tenants in common. Where two tenants in common incorporate, and the stock is equally divided between them, and they continue to deal with the property as tenants in common would do, the mere corporate form cannot be permitted to control the rights of the parties nor deprive them of a business advantage otherwise lawful.¹³

¹² Commerce Trust Co. v. McMe-
chen, — Mo. App. —, 220 S. W.
1019.

¹³ Cleveland-Cliffs Iron Co. v.
Arctic Iron Co., 261 Fed. 15, 18.

CHAPTER 13

CITIZENSHIP, DOMICILE, RESIDENCE AND HABITANCY

§ 387. In general.

§ 389. Equal privileges and immunities clause of Federal Constitution.

§ 390. For purposes of federal jurisdiction—Diversity of citizenship.

§ 391. —Suits for infringement of patents, and for wrongful use of trade-marks.

§ 397. For purposes of venue—Suits in state courts.

§ 398. Within statutes of limitations.

§ 399. For purposes of attachment and garnishment.

§ 403. “Principal place of business” and “residence” within bankruptcy acts.

§ 387. In general. A corporation is a “resident” of the state of its creation.¹ A corporation is domiciled in the state where created.²

§ 389. Equal privileges and immunities clause of Federal Constitution. A corporation is not a “citizen” within the federal “privileges and immunities” clause.³

§ 390. For purposes of federal jurisdiction—Diversity of citizenship. The citizenship of a corporation, for the purpose of jurisdiction of the federal courts, is in the state of its creation.⁴

¹ *Ryan v. Inyo Cerro Gordo Mining & Power Co.*, — Cal. App. —, 183 Pac. 250; *Jotter v. Charles B. Marvin Inv. Co.*, — Colo. —, 189 Pac. 22; *Republic Motor Truck Co. v. Buda Co.*, 212 Mich. 55, 179 N. W. 474; *Morris Plan Co. of Buffalo v. Miller*, 102 N. Y. Misc. 470, 169 N. Y. Supp. 37.

² *Pekin Cooperage Co. v. Duty*, 140 Ark. 135, 215 S. W. 715; *Mor-*

ris Plan Co. of Buffalo v. Miller, 102 N. Y. Misc. 470, 169 N. Y. Supp. 37.

³ *Adams v. American Agricultural Chemical Co.*, — Fla. —, 82 So. 850; *Bethlehem Motors Co. v. Flynt*, 178 N. C. 399, 100 S. E. 693.

⁴ *Everett Railway, Light & Power Co. v. United States*, 236 Fed. 806.

§ 391. — Suits for infringement of patents, and for wrongful use of trade-marks.⁵ A foreign corporation operating a plant employing several thousand men in a district where it is alleged to have infringed patents has a "regular and established place of business" in said judicial district, for jurisdictional purposes, under the federal statutes, although the principal place of business is in another state.⁶

§ 397. For purposes of venue—Suits in state courts. In California, a foreign corporation doing business in the state does not establish a residence in any particular county, such as is contemplated by the statutes relating to place of trial.⁷

§ 398. Within statutes of limitations. A foreign corporation is not absent from the state, so as to stop the running of limitations, where it is doing business in the state through a domestic corporation as its agent.⁸

§ 399. For purposes of attachment and garnishment.⁹

§ 403. "Principal place of business" and "residence" within bankruptcy acts. The principal place of business of a corporation, so far as the right to file an involuntary petition of bankruptcy against it is concerned, is not necessarily where the manager happens to be located nor where the stock book and record book are kept, although they are significant facts, but is to be gathered from a general survey of the corporation's activities.¹⁰

⁵ What constitutes "place of business" within federal statutes as to jurisdiction of infringement suits, see *American Elec. Welding Co. v. Lalanc & Grosjean Mfg. Co.*, 256 Fed. 34.

"Regular and established place of business," in infringement suit, as place where automobile company granted exclusive right to sell its cars in certain territory, see *Rosenbluth v. Hudson Motor Car Co.*, 265 Fed. 680.

⁶ *McKinnon Chain Co. v. American Chain Co.*, 259 Fed. 873.

⁷ *Ryan v. Inyo Cerro Gordo Mining & Power Co.*, — Cal. App. —, 183 Pac. 250.

⁸ *Alley v. Bessemer Gas Engine Co.*, 262 Fed. 94.

⁹ See § 3129, *infra*.

¹⁰ *In re Worcester Footwear Co.*, 251 Fed. 760.

CHAPTER 14

CORPORATE EXISTENCE

I. NECESSITY FOR EXISTENCE

§ 404. Existence essential to corporate acts.

II. COMMENCEMENT, DURATION AND EXTENSION OF EXISTENCE

§ 406. Commencement of existence—Performance of conditions precedent.

§ 412. Extension and revival of charters—Extension under general laws.

III. PROOF OF EXISTENCE

§ 416. Necessity to prove incorporation.

§ 419. What must be proved—De facto corporate existence.

§ 422. Presumptions and prima facie proof—In general.

§ 423. — Use of name importing a corporation.

§ 425. Parol evidence of incorporation; reputation.

§ 432. Organization of corporation and performance of conditions precedent—Articles, certificates, letters patent, etc.

§ 433. — National banks.

§ 437. — Foreign corporations.

I. NECESSITY FOR EXISTENCE

§ 404. Existence essential to corporate acts.¹ A deed to a void organization known by a company name conveys no title.² An agreement to assign contracts to a corporation will not be specifically enforced where the corporation is not yet created.³

II. COMMENCEMENT, DURATION AND EXTENSION OF EXISTENCE

§ 406. Commencement of existence—Performance of conditions precedent. “Where certain acts are absolutely required to be performed before the corporation comes into existence, these are conditions precedent, and no corporation is created or can exist until those acts are performed.”⁴

¹ See also § 2936, *infra*.

³ *Meyer v. Kauffmann*, 105 N.

² *Lynch v. Calkins*, 75 Okla. 137, 182 Pac. 225.

Y. Misc. 512, 173 N. Y. Supp. 601.

⁴ *Parkside Cemetery Ass'n v.*

§ 412. Extension and revival of charters—Extension under general laws. The Missouri statute as to fees on extending the duration of a corporation is construed to apply both to corporations created before the statute and those created afterwards.⁵

III. PROOF OF EXISTENCE

§ 416. Necessity to prove incorporation. In a prosecution for an offense committed on the property of a corporation, proof that the company was legally incorporated is not necessary.⁶ Corporate existence of bank burglarized, as alleged in the indictment, need not be proved in a prosecution for burglary.⁷

§ 419. What must be proved—De facto corporate existence. When collaterally assailed, it is sufficient to prove that the corporation has a de facto existence.⁸

§ 422. Presumptions and prima facie proof—In general. Proceeding to act as a corporation, it seems, raises a presumption of incorporation.⁹ The execution of contracts in which the other party to the contract is called a corporation is sufficient evidence against the party to the contract that the other party was a corporation.¹⁰ In an action on a contract, the written contract, showing that the defendant was dealing with the plaintiff as a corporation, is competent against defendant as evidence of corporate existence.¹¹ Proof of corporate existence of defendant is sufficient in an attachment suit where the attach-

Cleveland, B. & G. Lake Traction Co., 93 Ohio St. 161, Ann. Cas. 1918 C 1051, 112 N. E. 596, and see § 182 et seq., supra.

⁵ State ex rel. Kinloch Tel. Co. v. Roach, 269 Mo. 437, 190 S. W. 862, and see § 225, supra.

⁶ State v. Keech, 103 Wash. 533, 175 Pac. 176.

⁷ Moore v. State, — Ga. App. —, 102 S. E. 916.

⁸ Brinkley-Douglas Fruit Co. v. Silman, 33 Cal. App. 643, 166 Pac. 371.

⁹ Stauffer v. Koch, 225 Mass. 525, 114 N. E. 750.

Where land is conveyed to a company as a corporation, and it undertakes, by its president and secretary, as such corporation, to convey such land to another, it will be presumed that the company was regularly incorporated and that its officers were authorized to make the deed. Cotton v. White, 131 Ark. 273, 199 S. W. 116.

¹⁰ Zehr v. Zehr, 203 Ill. App. 584.

¹¹ Otis Elevator Co. v. Cape Fear Hotel Co., 172 N. C. 319, 90 S. E. 253.

ment bond containing a recital of the corporate existence of defendant is introduced in evidence.¹² Direct and positive evidence that a body is a voluntary and unincorporated association overthrows any presumptions in favor of the existence of a corporation.¹³ Of course there is no presumption that two persons are a corporation.¹⁴

§ 423. — **Use of name importing a corporation.** The word "company" as used in a statute does not necessarily mean a corporation.¹⁵ In the absence of evidence to the contrary, it will be presumed that the name "Tindle Cotton Company" is that of a corporation and not a firm.¹⁶ The name "V. M. Barrett Construction Company" imports that such company is a corporation.¹⁷ Addressing a company as the "Fidelity Electric Company, Inc." is some evidence against the person so addressing that the company was a corporation.¹⁸ The name "Bremen Foundry & Machine Works" clearly indicates that it is not a natural person but is a corporation or a partnership.¹⁹ The name "Mexico American Colony Association" on the office door does not necessarily constitute notice of the existence of a corporation.²⁰

§ 425. **Parol evidence of incorporation; reputation.** Corporate existence may be proved by parol, in a proper case,²¹ as where called in question collaterally,²² or where the charter has been lost or mislaid.²³

¹² *Burke v. Barnum & Bailey*, 40 R. I. 71, 99 Atl. 1027.

¹³ *Simpson v. Grand International Brotherhood of Locomotive Engineers*, 83 W. Va. 355, 98 S. E. 580.

¹⁴ *Kreuger v. State*, 82 Tex. Cr. 404, 199 S. W. 629.

¹⁵ *Harger v. Harger*, — Ark. —, 222 S. W. 736, and see § 336, *supra*.

¹⁶ *Pemiscot County Bank v. Central State Nat. Bank*, 135 Tenn. 13, 185 S. W. 702.

¹⁷ *Hunnicut v. Reed*, 149 Ga. 803, 102 S. E. 421.

¹⁸ *Stauffer v. Koch*, 225 Mass. 525, 114 N. E. 750.

¹⁹ *Bremen Foundry & Machine Works v. Boswell*, 22 Ga. App. 434, 96 S. E. 182.

²⁰ *Luck v. Alamo Printing Co.*, — Tex. Civ. App. —, 190 S. W. 204.

²¹ *Brinkley-Douglas Fruit Co. v. Silman*, 33 Cal. App. 643, 166 Pac. 371; *Landis v. State*, 85 Tex. Cr. 381, 214 S. W. 827; *Umpqua Valley Fruit Union v. North Pacific Fruit Distributors*, 108 Wash. 265, 183 Pac. 101.

²² *Farmers' Nat. Bank v. Johnston*, — Okla. —, 3 A. L. R. 99, 176 Pac. 236.

²³ *Carrell v. State*, 84 Tex. Cr. 554, 209 S. W. 158.

§ 432. **Organization of corporation and performance of conditions precedent—Articles, certificates, letters patent, etc.** The articles of incorporation are admissible, where properly authenticated, to show the corporate entity of the plaintiff.²⁴ The articles, etc., of incorporation are the best evidence of the fact of incorporation.²⁵ The production of the charter makes a prima facie case of corporate existence.²⁶

§ 433. — **National banks.**²⁷

§ 437. — **Foreign corporations.**²⁸

²⁴ Collins v. Armour Fertilizer Works, 18 Ga. App. 533, 89 S. E. 1054.

²⁵ Daniel v. Wade, — Ala. —, 83 So. 99.

²⁶ La Salle v. Hamilton Nat. Bank, 204 Ill. App. 518.

²⁷ “Mode of proving corporate existence of national bank,” see note in 3 A. L. R. 101, annotating Farmers’ Nat. Bank v. Johnston, — Okla. —, 3 A. L. R. 99, 176 Pac. 236.

²⁸ See § 5975, *infra*.

CHAPTER 15

UNDERWRITING AGREEMENTS

§ 443. Distinctions.

§ 445. Form of agreement.

§ 443. Distinctions.¹

§ 445. Form of agreement.² The reservation by a subscriber of the privilege of paying for his stock before the time when the underwriting was intended to be dissolved does not relieve him of his equal obligation under the contract, and the exercise of such option does not increase the responsibility of the other subscribing parties.³

¹ Syndicate agreements as similar, see *Gates v. Megargel*, 266 Fed. 811.

² Construction of agreement, see *Wing v. Sedgwick*, 254 Fed. 5; *Wing v. McCallum*, 244 Fed. 199;

Bucher v. Federal Baseball Club of Baltimore, 130 Md. 635, 101 Atl. 534.

³ *Bucher v. Federal Baseball Club of Baltimore*, 130 Md. 635, 101 Atl. 534.

CHAPTER 16

BY-LAWS

I. DEFINITION AND DISTINCTIONS

§ 481. Distinguished from resolutions.

II. ADOPTION AND PROOF

§ 484. Adoption—Power in general.

§ 486. — By whom power exercised.

§ 487. — Mode.

III. VALIDITY

§ 489. Consonance with law.

§ 492. Impairment of obligation of contracts and destruction or impairment of vested rights.

§ 493. Restraint of trade.

§ 494. Consonance with charter and with nature, purposes and objects corporation.

§ 495. Reasonableness.

IV. CONSTRUCTION

§ 499. General rules as to construction.

V. NOTICE

§ 500. Presumption of knowledge.

VI. OPERATION AND EFFECT

§ 501. On stockholders or members.

§ 502. On third persons.

VII. WAIVER

§ 503. Power of corporation, members and officers as to waiver of by-laws; proof of waiver.

VIII. AMENDMENT AND SUBSEQUENT ADOPTION.

§ 504. Power in general.

IX. REPEAL

§ 508. Power in general.

§ 510. Mode.

X. REGULATION OF PARTICULAR MATTERS

§ 512. Stock; issue; payment; assessments; rights and liabilities of stockholders in general.

§ 513. Transfer of stock—Restrictions on alienation.

§ 514. — Protective regulations.

§ 515. — Creating or reserving lien on stock.

I. DEFINITION AND DISTINCTIONS

§ 481. Distinguished from resolutions.¹

II. ADOPTION AND PROOF

§ 484. Adoption—Power in general.²

§ 486. — **By whom power exercised.** “Ordinarily by-laws are made by the stockholders, but, where the statute gives that power to the board of directors, the stockholders cannot change it or interfere with the board in this particular so long as such by-laws are reasonable and do not interfere with the vested and substantial rights of the stockholders, or are not contrary to public policy or the established law of the land.”³ “There is no reason why the stockholders of a corporation may not ratify by-laws adopted by the promoters before letters patent have been issued and delivered to it.”⁴ “The majority [stockholders] have the right to impose upon the minority additional by-laws not inconsistent with the charter.”⁵

§ 487. — **Mode.** The plan of organization of a fraternal benefit society, as set forth in its constitution, is not amendable by a by-law not enacted pursuant to the provision of the

¹ See § 492, *infra*.

² In Alabama, however, it is said that “the charter does not authorize any such by-law and its adoption is therefore *ultra vires*.” *Baldwin County Producers’ Corporation v. Frishkorn*, — Ala. App. —, 81 So. 862.

³ *State ex rel. Daubenspeck v. Day*, — Ind. —, 123 N. E. 402.

⁴ *National Surety Co. v. Williams*, 74 Fla. 446, 77 So. 212.

⁵ *G. W. Jones Lumber Co. v. Wisarkana Lumber Co.*, 125 Ark. 65, 187 S. W. 1068.

constitution as to amendments.⁶ A contract of a member to be bound by future enacted by-laws means such by-laws as may be legally enacted, whether in the manner provided at the date of his membership or in some other legal manner thereafter provided.⁷

III. VALIDITY

§ 489. Consonance with law. By-laws contrary to the common or statutory law of the country are void.⁸ If by-laws and a statute conflict, the statute prevails.⁹ Thus, a by-law defining a quorum is invalid where in conflict with a statute.¹⁰

§ 492. Impairment of obligation of contracts and destruction or impairment of vested rights. A by-law increasing the liability of stockholders, as by imposing liability for past and future debts, is invalid.¹¹ Resolutions of the Chicago Board of Trade, affecting prior contracts of its members, are not "laws" within the constitutional prohibition of laws impairing the obligation of contracts.¹²

§ 493. Restraint of trade. A by-law in restraint of trade is unenforceable.¹³ Thus, a by-law of a grain buying company

⁶ Kirkpatrick v. Abrahams, 98 Kan. 685, 159 Pac. 13.

⁷ Apitz v. Supreme Lodge, 196 Ill. App. 278.

⁸ State ex rel. Black v. Aztec Ditch Co., 25 N. M. 590, 185 Pac. 549, citing 1 Fletcher's Cyc. Corp. § 488; Murphy v. Moncton Hospital, 35 Dom. L. Rep. (Can.) 327.

A by-law is invalid where opposed to the law of the land. Gaffney v. Royal Neighbors of America, 31 Idaho 549, 174 Pac. 1014.

By-laws must not be contrary to the general statutes or charter provisions. Wegener v. Wegener, — Ohio St. —, 126 N. E. 892.

"It is uniformly held that a by-law of a private corporation

* * *, in order to be valid, must be consistent with the law of the land, and a by-law or ordinance in contravention of a statute of the state is invalid." State ex rel. Black v. Aztec Ditch Co., 25 N. M. 590, 185 Pac. 549, quoting Fletcher's Cyc. Corp.

⁹ Grant v. Elder, 64 Colo. 104, 170 Pac. 198.

¹⁰ In re P. F. Keogh, 192 N. Y. App. Div. 624, 183 N. Y. Supp. 408.

¹¹ Roush v. Longdale Independent Tel. Co., 78 W. Va. 136, 88 S. E. 623.

¹² Thomson v. Thomson, 293 Ill. 584, 127 N. E. 882.

¹³ Baldwin County Producers' Corporation v. Frishkorn, — Ala. App. —, 81 So. 862; Booker &

whereby farmers agree not to sell their grain to competitors of their own company, except on payment of a penalty of one cent a bushel, is unreasonable and invalid from the viewpoint of a contract as in restraint of trade.¹⁴

§ 494. Consonance with charter and with nature, purposes and objects of corporation. The nature of a corporation as evidenced by its articles of incorporation cannot be affected by its by-laws.¹⁵

§ 495. Reasonableness. By-laws are not invalid because their effect is to limit the freedom of action of members and to injure the business of third persons.¹⁶ A by-law of a fraternal benefit society is not valid if it is unreasonable.¹⁷

IV. CONSTRUCTION

§ 499. General rules as to construction. Conflicts between provisions of the by-laws of a fraternal benefit society are to be resolved in the same manner as conflicts between statutes.¹⁸

Kinnaird v. Louisville Board of Fire Underwriters, 188 Ky. 771, 224 S. W. 451.

By-law as in restraint of trade, see *Ex Parte Baldwin County Producers' Corporation*, — Ala. —, 83 So. 69.

¹⁴*Burns v. Wray Farmers' Grain Co.*, 65 Colo. 425, 176 Pac. 487, approving *Reeves v. Decorah Farmers' Co-Op. Society*, 160 Iowa 194, 44 L. R. A. (N. S.) 1104, 140 N. W. 844.

A by-law of a co-operative corporation providing that "a member of the corporation selling his produce to any person other than the regularly authorized agent of the corporation shall pay three per cent of his gross sales into the treasury of the corporation" is unenforceable because in restraint of trade. *Baldwin County Pro-*

ducers' Corporation v. Frishkorn, — Ala. App. —, 81 So. 862.

¹⁵*Canyon Creek Irrigation Dist. v. Martin*, 52 Mont. 339, 159 Pac. 418.

¹⁶*Booker & Kinnaird v. Louisville Board of Fire Underwriters*, 188 Ky. 771, 224 S. W. 451.

¹⁷*Sovereign Camp of Woodmen of World v. Robinson*, — Tex. Civ. App. —, 187 S. W. 215.

By-laws of Knights of Pythias held unreasonable, see *Supreme Lodge v. Wilson*, — Tex. Civ. App. —, 204 S. W. 891.

Reasonableness of by-law of co-operative farmers' association as to mode of distributing profits among members, see *Mooney v. Farmers' Mercantile & Elevator Co. of Madison*, 138 Minn. 199, 164 N. W. 804.

¹⁸*Kirkpatrick v. Abrahams*, 98 Kan. 685, 159 Pac. 13.

V. NOTICE

§ 500. Presumption of knowledge.¹⁹ "It cannot be presumed that a transferee of stock in a corporation has knowledge of the corporation by-laws." This was said in an action by a purchaser of stock to compel a foreign corporation to transfer the stock on its books to him.²⁰

VI. OPERATION AND EFFECT

§ 501. On stockholders or members. By-laws, when adopted, are as much the law of the corporation as if the provisions thereof had been a part of the charter.²¹ Members of a fraternal insurance society are bound by valid by-laws.²² A by-law violating a statute is void as to a member chargeable with knowledge of the corporate want of power to make a contract based thereon.²³

§ 502. On third persons.²⁴ Third persons are not bound by by-laws not expressly authorized by the charter or statute unless they have actual notice of them.²⁵ However, even verbal by-laws are binding on the payee of a note made by a corporation, where he knows of such by-laws.²⁶ A general manager employed for a year with knowledge of a by-law giving the board of directors power to remove the manager when deemed necessary for the best interests of the company, is bound by such by-law and cannot recover where discharged by the directors before the end of the year.²⁷

¹⁹ See also §§ 501, 502.

²⁰ *Baer v. Waseca Milling Co.*, 143 Minn. 483, 171 N. W. 767, 173 N. W. 401.

²¹ *Kavanaugh v. Commonwealth Trust Co. of New York*, 223 N. Y. 103, 119 N. E. 237.

²² *Weiditschka v. Supreme Tent Knights of Maccabees of World*, — Iowa —, 170 N. W. 300.

²³ *Haner v. Grand Lodge A. O. U. W.*, 102 Neb. 563, 168 N. W. 189.

²⁴ By-laws as notice of powers of officers or agents to third persons dealing with corporation, see § 1926, *infra*.

²⁵ *Newton v. Johnston Organ & Piano Mfg. Co.*, — Cal. —, 180 Pac. 7.

²⁶ *Phillips v. Interstate Land Co.*, 174 N. C. 542, 94 S. E. 12.

²⁷ *Rundell v. Farmers' Co-Op. Elevator Co.*, 210 Mich. 642, 178 N. W. 21.

VII. WAIVER

§ 503. Power of corporation, members and officers as to waiver of by-laws; proof of waiver. Nonusage of a by-law by corporate officers, continued for a sufficient length of time to bring it home to the stockholders, will work its abrogation.²⁸

VIII. AMENDMENT AND SUBSEQUENT ADOPTION

§ 504. Power in general. Conceding that a custom of distributing profits equally among stockholders became in legal effect a by-law, the custom may be abandoned or modified precisely the same as a formally enacted by-law may be amended or wholly repealed.²⁹ Equity has jurisdiction to cancel an invalid amendment of a by-law.³⁰

IX. REPEAL

§ 508. Power in general. Even if a long continued custom is in effect a by-law, it may be abandoned precisely the same as a formally enacted by-law may be amended or wholly repealed.³¹ A by-law requiring notice of special corporate meetings cannot be arbitrarily revoked by the directors.³² By-laws adopted by the stockholders cannot be changed by the board of directors.³³

§ 510. Mode. By-laws provided that they could be amended or revoked by majority vote of the trustees "at any monthly meeting, notice being given at a previous meeting of any intended change, and that the change must not be acted upon for at least one month from the time of giving of notice." It was held that a repeal of a by-law at a regular meeting, without notice of any intended change, was effective from the next meeting over a month later when the same trustees approved the acts

²⁸ Huxtable v. Berg, 98 Wash. 616, 168 Pac. 187.

²⁹ Mooney v. Farmers' Mercantile & Elevator Co. of Madison, 138 Minn. 199, 164 N. W. 804.

³⁰ Roush v. Longdale Independent Tel. Co., 78 W. Va. 136, 88 S. E. 623.

³¹ Mooney v. Farmers' Mercantile & Elevator Co. of Madison, 138 Minn. 199, 164 N. W. 804.

³² Canada Furniture Co. v. Banning, 39 Dom. L. Rep. (Can.) 313.

³³ State ex rel. Carpenter v. Kreutzer, 100 Ohio St. 246, 126 N. E. 54.

of the preceding meeting.³⁴ The rule that "nonusage of a by-law by the corporate officers when continued for a length of time sufficient to bring it home to the stockholders will accomplish the abrogation thereof," was reiterated and applied by the Washington Supreme Court where a by-law providing that the annual rentals of an irrigation company should not exceed one dollar a share unless authorized by a majority vote of the stockholders, was violated by the corporate trustees who repeatedly, from year to year, fixed and collected a water rental of five to six dollars a share, without being authorized so to do by a majority vote of stockholders.³⁵

X. REGULATION OF PARTICULAR MATTERS

§ 512. Stock; issue; payment; assessments; rights and liabilities of stockholders in general. In Minnesota, the statutes authorize co-operative associations to provide by by-law for the distribution of profits and earnings in such proportions as the stockholders may deem just. Pursuant thereto a by-law of a farmers' co-operative mercantile company provided for equal distribution of profits among the stockholders up to seven per cent and a division of the balance of profits among the stockholders "pro rata to the amount of business each has furnished to the company during the year, in the form of furnishing to it the product or products in which it is dealing." A stockholder who contributed nothing to the business of the company attacked the by-law as violating his vested rights because of a long-continued custom of distributing the profits in equal proportions to all stockholders, but the by-law was held valid.³⁶ A by-law providing that no assessment shall be levied while any portion of the previous one remains unpaid unless the power of the corporation for collecting it has been exercised or the collecting has been enjoined, is for the protection of those who have paid their assessments and does not mean "that one who fails to pay an assessment against his stock thereby exempts himself from any further assessment."³⁷

³⁴ Pennecard v. Giant Ledge tile & Elevator Co. of Madison, Min. Co., 97 Wash. 384, 166 Pac. 629. 138 Minn. 199, 164 N. W. 804.

³⁵ Huxtable v. Berg, 98 Wash. 616, 168 Pac. 187. ³⁷ Pennecard v. Giant Ledge Min. Co., 97 Wash. 384, 166 Pac. 629.

³⁶ Mooney v. Farmers' Mercan-

§ 513. Transfer of stock—Restrictions on alienation. There is a special reason why by-law restrictions on the power to transfer stock should be upheld in the case of “co-operative” companies as distinguished from ordinary business corporations.³⁸ Charter power of a co-operative company, not only to regulate the right to transfer stock but also to make by-laws as to “the terms and limitations of stock ownership,” especially where the corporation is authorized to purchase its own stock, confers power to adopt a by-law providing that no stockholder shall transfer his stock without giving the corporation 90 days’ notice and an option to purchase the stock at par plus dividends.³⁹ Power to make by-laws regulating “the transfer of stock” does not authorize a by-law to permit directors to veto such transfers.⁴⁰ A by-law authorizing directors to refuse arbitrarily to transfer shares of stock is invalid in Canada.⁴¹

§ 514. — Protective regulations. A by-law providing that stock “shall after payment of all calls or assessments thereon be transferable on the books of the company” means that the stock shall be transferable after the payment of all calls or of all instalments then due upon such calls.⁴²

§ 515. — Creating or reserving lien on stock. The transferee of stock is not affected by the terms of a by-law as to a lien of which he has no notice, where the certificate makes no reference thereto.⁴³ The contract lien of a pledgee of stock, dating from the execution of the contract, is superior to a by-law lien of the corporation, where the pledgee had no notice thereof until sale of the stock to enforce the pledge.⁴⁴ The words “transferable only on the books of the corporation in person or by attorney on surrender of this certificate,” in a stock certificate, do not charge the transferee with notice of a by-law lien.⁴⁵

³⁸ *Chaffee v. Farmers’ Co-Op. Elevator Co.*, 39 N. D. 585, 168 N. W. 616.

³⁹ *Chaffee v. Farmers’ Co-Op. Elevator Co.*, 39 N. D. 585, 168 N. W. 616.

⁴⁰ *Canada National Fire Ins. Co. v. Hutchings*, 39 Dom. L. Rep. (Can.) 401.

⁴¹ *Hutchings v. Canadian Nat. Fire Ins. Co.*, 33 Dom. L. Rep. (Can.) 752, 750.

⁴² *Geary St., P. & O. R. Co. v. Bradbury Estate Co.*, 179 Cal. 46, 175 Pac. 457.

⁴³ *Citizens’ Bank of Maxeys v. Bank of Penfield*, — Ga. App. —, 101 S. E. 203.

⁴⁴ *American Nat. Bank of Atlanta v. East Atlanta Bank*, 147 Ga. 750, 95 S. E. 286.

⁴⁵ *Citizens’ Bank of Maxeys v. Bank of Penfield*, — Ga. App. —, 101 S. E. 203.

CHAPTER 17

SUBSCRIPTIONS TO CAPITAL STOCK

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- § 521. Formation of contract of subscription—In general.
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- § 556. Authority and duties generally as to receiving subscriptions.
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- § 568. Illegality in contracts of subscription.
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- § 570a [New]. Equities of subscriber as inferior to rights of creditor.
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XIII. ESTOPPEL OF SUBSCRIBERS

§ 716. Estoppel to deny subscription or the validity thereof.

I. NATURE AND FORMATION OF CONTRACTS OF SUBSCRIPTION AND OTHER AGREEMENTS

§ 520. Subscriptions and other agreements defined and distinguished. A subscription for stock is distinguishable from a contract to purchase stock.¹ Where one purchases stock from another who holds it in trust, but deals with the individual and not with the corporation, he is not a subscriber.² Purchase of preferred stock from the president of the corporation, where all the preferred stock had been issued to him for contracts held by him, is not a subscription to stock although full value was not paid.³ A statute prohibiting the carrying on of "business" before filing specified papers does not apply to the taking of stock subscriptions.⁴

The provision of the Michigan Securities Act excluding from its operation everything relating to the issuance of stock by a corporation to the "original subscribers to its articles of incorporation" excludes matters relating to the issuance of stock to subscribers to the capital stock before incorporation but who did not actually sign the articles of incorporation.⁵

§ 520a [New]. Permit as condition precedent under Blue Sky Law. Under the California Blue Sky Law, no valid subscription to stock can be made before a permit is secured from the commissioner of corporations.⁶

§ 521. Formation of contract of subscription—In general. Acceptance by the corporation is necessary to constitute a bind-

¹ Mills v. Friedman, 111 N. Y. Misc. 253, 181 N. Y. Supp. 285.

² Rochelle Roofing Co. v. Burley & Stevens, 226 Mass. 349, 115 N. E. 478.

³ Rochelle Roofing Co. v. Burley & Stevens, 226 Mass. 349, 115 N. E. 478.

⁴ Hauger v. International Trading Co., 184 Ky. 794, 214 S. W. 438.

⁵ Decke v. Baker, 201 Mich. 608, 167 N. W. 908.

⁶ Nannizzi v. Caprile, — Cal. App. —, 185 Pac. 673.

ing subscription,⁷ but it is not necessary that a stock certificate be issued.⁸ A subscription for a specified number of shares is a continuing offer until accepted or revoked.⁹ Acceptance of a subscription contract by the corporation need not be formal.¹⁰ Receipt of notice of a shareholders' meeting by a subscriber for shares is notice of acceptance of his application for shares.¹¹ A formal allotment of shares or sending a notice of allotment is not necessary to make a subscriber a stockholder.¹²

§ 522. — Subscriptions after formation of corporation.¹³

Where a prospective subscriber to stock refused to pay anything down but proposed that he be given the option to return the stock within 10 months and receive back his note or any cash paid, and the agent agreed to submit this proposition to the company but did not do so but instead turned in the subscription as an unconditional one, the subscriber is not liable on the subscription because no contract was ever entered into.¹⁴

§ 523. — Subscriptions before formation of corporation.

Subscriptions before incorporation become binding as soon as the corporation is formed and it expressly or impliedly accepts them.¹⁵ Subscriptions to stock fully carried out before the creation of the corporation bind both the subscriber and the after-created corporation.¹⁶ Postponement of acceptance of a subscription to stock, after organization of the corporation, is not a rejection of the subscription.¹⁷

⁷ *Natwick v. Terwilliger*, 24 Wyo. 253, 160 Pac. 338.

⁸ *Jackson v. Sabie*, 36 N. D. 49, 161 N. W. 722.

⁹ *Martin v. Cushwa*, — W. Va. —, 104 S. E. 97.

¹⁰ *Re Monarch Bank of Canada*, 48 Dom. L. Rep. (Can.) 588.

¹¹ *Traders Trust Co. v. Goodman*, 37 Dom. L. Rep. (Can.) 31.

¹² *Alberta Rolling Mills Co. v. Christie*, 45 Dom. L. Rep. (Can.) 545, rev'g 38 Dom. L. Rep. 488.

¹³ See also § 521, *supra*.

¹⁴ *Tidewater Southern R. Co. v. Merz*, 35 Cal. App. 405, 169 Pac. 1054.

¹⁵ *Martin v. Rothwell*, 81 W. Va. 681, 95 S. E. 189.

In Canada, a subscription to stock in a company not yet incorporated must be accepted by an allotment of the shares applied for and a notice to the subscriber of such allotment. *Morse Co-Operative Supply Co. v. Coates*, 38 Dom. L. Rep. (Can.) 92.

¹⁶ *Stone v. Walker*, 201 Ala. 130, L. R. A. 1918 C 839, 77 So. 554.

¹⁷ *Martin v. Cushwa*, — W. Va. —, 104 S. E. 97.

§ 524. — **Formation of a different corporation.** Where the objects of the corporation formed were wholly different from those specified in the subscription contract, the subscriber cannot be held liable.¹⁸ However, a material change in the character of the enterprise or purpose of a proposed corporation does not release a subscriber. Only a material change in the charter of the corporation, made without his consent, will release him.¹⁹

§ 526. **Consideration and mutuality—In general.** Stock subscriptions are not binding where based on no consideration,²⁰ but opportunity to buy stock is a consideration for the agreement to purchase,²¹ and mutual promises of subscribers are a sufficient consideration in states where a subscription by a number of persons to stock in a company to be thereafter formed by them is regarded as a contract between the subscribers.²² There need be no certificate of stock issued in order to constitute a consideration for a subscription to stock.²³ If the stock is of no value whatever when purchased, there is no consideration. It is a defense to an action on a stock subscription note.²⁴

Fictitious subscriptions to stock are unlawful and the subscriber cannot recover sums paid as advances.²⁵

§ 528. — **Failure of consideration.**²⁶ The fact that stock became worthless or deteriorated in value is not ground for

¹⁸ *Collings v. Allen*, 90 N. J. L. 5, 100 Atl. 170, aff'd without opinion, 102 Atl. 1052.

Objection that a corporation was not the kind contemplated by the subscription held not sustained in *Philadelphia Motor Speedway Ass'n v. Sale*, 69 Pa. Super. Ct. 583.

¹⁹ *Bunn v. Farmers' Warehouse Co.*, 18 Ga. App. 567, 90 S. E. 78.

²⁰ *Baldwin v. Timber Inv. Co.*, — N. D. —, 176 N. W. 662.

²¹ *Nolle v. Mutual Union Brewing Co.*, 264 Pa. 534, 108 Atl. 23.

²² *Philadelphia Motor Speedway Ass'n v. Sale*, 69 Pa. Super. Ct. 583.

²³ *Skluzacek v. Fossum*, 139 Minn. 498, 166 N. W. 124.

²⁴ *Lindsay v. Sonora Gold Mining & Milling Co.*, — Mo. —, 196 S. W. 764.

²⁵ *Henderson v. Strang*, 48 Dom. L. Rep. (Can.) 606.

²⁶ See also § 654, *infra*.

For note on "Right to recover money paid to a corporation in expectation of receiving corporate stock which is never issued," see L. R. A. 1918 E 754, annotating *Clark v. Hamilton*, 217 Fed. 229, L. R. A. 1918 E 750.

rescission where it was really of the value stated at the time of the sale.²⁷ A promise to employ a subscriber to stock "permanently," as part of the consideration for his subscription, is not broken where he continued in its employment until the corporation was dissolved.²⁸

§ 529. Incomplete subscriptions.²⁹

§ 532. Subscription paper as contract between subscribers.³⁰

§ 534. Form of subscription and formalities in subscribing—In general. It is well settled "that a contract for an original issue of shares of stock in exchange for property is in legal effect but a subscription to stock, even if it be not a subscription contract in form."³¹

§ 535. — Definiteness and certainty; misnomer.³² Omitting "Inc." from the corporate name does not affect the validity of a subscription to the company, where no question of identity is involved.³³

§ 537. — Necessity for writing—Statute of frauds.³⁴ A parol subscription to stock is valid, in the absence of a statute to the contrary.³⁵ A subscription is not within the statute of frauds, as an agreement for the sale of goods, wares or merchandise.³⁶

On the other hand, an agreement for sale of stock in a corporation to be formed, where not capable of performance in a year, is within the statute of frauds.³⁷ But deferred payments

²⁷ *Palmer v. Citizens' Bank of Murray*, 179 Ky. 54, 200 S. W. 41.

²⁸ *Beeman v. Richardson*, — Cal. App. —, 189 Pac. 790.

²⁹ Parol evidence as to, see § 569, *infra*.

³⁰ Necessity for acceptance of subscription, see §§ 521-523, *supra*.

³¹ *Pasadena Rapid Transit Co. v. Munson*, 37 Cal. App. 352, 174 Pac. 109.

³² Particular subscription agreement held not to show an enforceable contract, performance of

which could be specifically enforced, in *Jamestown Portland Cement Corporation v. Bowles*, 228 Mass. 176, 117 N. E. 41.

³³ *Mechanicville War Chest v. Butterfield*, 110 N. Y. Misc. 257, 181 N. Y. Supp. 428.

³⁴ See also § 696, *infra*.

³⁵ *Mills v. Friedman*, 111 N. Y. Misc. 253, 181 N. Y. Supp. 285.

³⁶ *Mills v. Friedman*, 111 N. Y. Misc. 253, 181 N. Y. Supp. 285.

³⁷ *Meyer v. E. G. Spink Co.*, — Ind. App. —, 124 N. E. 757.

on a stock subscription are enforceable even if the contract is not in writing and such payments extend beyond the period of one year.³⁸

§ 543. Subscriptions implied from conduct. The taking of certificates of stock without subscription implies a promise to pay for them.³⁹

§ 544. Effect of mistake or ignorance. Mistake may authorize reformation of a stock subscription so as to make it conditional rather than absolute.⁴⁰

§ 549. Capacity of subscribers and effect of disability—Subscriptions by municipal corporations. The legislature may authorize cities and towns to subscribe for railroad stock.⁴¹

§ 551. — Subscriptions by officers, agents and commissioners. An optional subscription to stock, made by the promoters of the corporation and ratified by themselves as the board of directors, with no intention of enforcing it unless the corporation was a success, but held out to the public as a binding subscription, is a fraud on future subscribers and cannot be enforced against the corporation.⁴²

§ 553. Subscriptions by agents, trustees or partners.⁴³ An executor cannot bind the estate by subscribing for stock.⁴⁴

§ 556. Authority and duties generally as to receiving subscriptions. If a subscriber pay money to an authorized agent who embezzles it, and no stock is ever delivered to the subscriber, it seems that the subscriber may recover from the cor-

³⁸ Benner v. Billings, 107 Wash. 1, 181 Pac. 19.

³⁹ Campbell v. Coin Mach. Mfg. Co., — Ore. —, 188 Pac. 197.

⁴⁰ See Hauger v. International Trading Co., 184 Ky. 794, 214 S. W. 438.

⁴¹ In re Opinion of Justices, 231 Mass. 603, 122 N. E. 763.

⁴² Ennis v. New World Life Ins. Co., 97 Wash. 122, 165 Pac. 1091.

⁴³ A testamentary trustee not limited, by express declaration of the will, to the usual investments of trust estates, may, it seems, invest in good railroad stocks. In re United States Trust Co. of New York, 189 N. Y. App. Div. 75, 178 N. Y. Supp. 125.

⁴⁴ Lovenskiold v. Nueces Hotel Co., — Tex. Civ. App. —, 208 S. W. 759.

poration the amount paid the agent.⁴⁵ If a corporation after organization accepts a conditional subscription made before the corporation was created, it accepts it subject to the conditions attached.⁴⁶

§ 563. Revocation or withdrawal of subscriptions—Before acceptance by the corporation. Until the corporation is formed, a subscriber is at liberty, it is held in Montana, to withdraw at any time.⁴⁷

§ 567. Lapse or abandonment of subscriptions.⁴⁸

§ 568. Illegality in contracts of subscription. The subscription may be void because in violation of the Blue Sky Law.⁴⁹ Where the project for which the corporation was formed turns out to be illegal, subscribers may repudiate their subscriptions if they act promptly.⁵⁰ Where a pretended corporation was prohibited by law, stock subscriptions and the notes given therefor are void.⁵¹ A subscription contract whereby stock was sold at less than par, in violation of statute, is unenforceable by the corporation or its assignee, a co-promoter with defendant;⁵² and an agreement between a promoter and a stock subscriber whereby he is to pay less than the subscription price is not binding on the corporation or other subscribers.⁵³ A contract to work for a corporation for a certain number of shares of stock to be paid for out of the dividends is not illegal because it gives the corporation the right to take over such stock at par if the employee quit the service, and such a provision does not provide for a forfeiture.⁵⁴

A contract by which a corporation gives an option to take and pay for at a fixed price all the unissued shares of its capital

⁴⁵ *Mutual Loan Society v. Letson*, 200 Ala. 251, 76 So. 17.

⁴⁶ *Martin v. Rothwell*, 81 W. Va. 681, 95 S. E. 189.

⁴⁷ *Canyon Creek Elevator & Milling Co. v. Allison*, 53 Mont. 604, 165 Pac. 753.

⁴⁸ By failure to accept, see § 521, *supra*.

⁴⁹ *Edward v. Ioor*, 205 Mich. 617, 172 N. W. 620.

⁵⁰ *Central Life Securities Co. v. Smith*, 236 Fed. 170.

⁵¹ *Davis v. Allison*, — Tex. Civ. App. —, 189 S. W. 968.

⁵² *Tramp v. Marquesen*, — Iowa —, 176 N. W. 977.

⁵³ *Lumpp v. Drumheller*, — Wash. —, 188 Pac. 913.

⁵⁴ *Williams v. Maryland Glass Corporation*, 134 Md. 320, 106 Atl. 755.

stock does not violate the rule against perpetuities.⁵⁵ A contract between a corporation and an individual giving the latter the exclusive right to take at par one hundred thousand dollars of shares of the company, without limit of time, such option covering nearly half the capital stock, cannot be attacked by persons subsequently acquiring stock in the corporation although they did not know about such contract; and where such contract was assigned to one who loaned money to the company to extend its business, the result of which was highly beneficial, a third person cannot attack the contract as oppressive because the stock sold above par. Moreover, the rule against perpetuities does not apply since such rule should not be extended to stock of a private business corporation.⁵⁶ In New York, however, it is held that an option given by a corporation to purchase its stock at par at a future time, without regard to market value at the time, is speculative and may be void as a fraud on innocent subscribers and as against public policy, and is not validated as to the balance by an exercise of the option as to part of the stock.⁵⁷

If the subscription is void because of violation of statute, the subscriber may rescind and recover back what he has parted with.⁵⁸ In such a case, a subscriber may recover back the amount paid because of want of consideration, and the rule that an ultra vires contract fully executed cannot be attacked is not applicable.⁵⁹ An offer to surrender the illegal certificate of stock and a demand of a return of the money paid for the stock is sufficient without also making a specific offer to return dividends received.⁶⁰

§ 569. Proof of subscriptions.⁶¹ A certified copy of the articles of incorporation is admissible to show who were subscribers to the capital stock of a corporation,⁶² and the stock

⁵⁵ *Kingston v. Home Life Ins. Co. of America*, — Del. Ch. —, 101 Atl. 898.

⁵⁶ *Kingston v. Home Life Ins. Co. of America*, — Del. Ch. —, 101 Atl. 898.

⁵⁷ *Donovan v. Powers Film Products*, 111 N. Y. Misc. 276, 181 N. Y. Supp. 157.

⁵⁸ *Edward v. Ioor*, 205 Mich. 617, 172 N. W. 620.

⁵⁹ *Heide v. Capital Securities Co.*, 200 Ala. 397, 76 So. 313.

⁶⁰ *Heide v. Capital Securities Co.*, 200 Ala. 397, 76 So. 313.

⁶¹ Parol evidence to contradict or vary, see § 609, *infra*.

⁶² *Sunshine Laundry Co. v.*

record of a bank is admissible to prove that defendant was a stockholder at a certain time.⁶³ The transfer book is the best evidence of stock ownership,⁶⁴ but a person whose name is not on the stock book may show that he is a stockholder.⁶⁵

If a stock subscription is incomplete as to when the stock was to be issued and delivered, parol evidence as to the understanding of the parties is admissible.⁶⁶ Thus, parol evidence is admissible, in such a case, to show that the stock was not to be delivered until the note given therefor was paid.⁶⁷

§ 570. Construction of subscription contracts.⁶⁸ An option on mining stock to be taken and paid for "in such sums and amounts as may be required in the prosecution of the work of development" is terminated when the mine becomes self-supporting.⁶⁹ A stock subscription payable in "securities" satisfactory to the insurance department means securities constituting property and which are proper to be used in payment.⁷⁰

§ 570a [New]. Equities of subscriber as inferior to rights of creditor. The equities of a subscriber to stock are, at least in Colorado, inferior to the rights of creditors who became such after the subscription.⁷¹

§ 571. General nature and extent of subscriber's liability.⁷² A subscriber's liability is contractual,⁷³ and is controlled by

Rhodes Avenue Hospital, 207 Ill. App. 19.

⁶³ *Bundy v. Wilson*, — Colo. —, 180 Pac. 740.

⁶⁴ *Farmers' State Bank v. Tri-State Mut. Grain Dealers' Fire Ins. Co.*, 41 S. D. 398, 170 N. W. 638.

In Delaware, the stock ledger is the only evidence as to who are stockholders entitled to vote. *Schultz v. Commonwealth Mortg. Co.*, — Del. Ch. —, 107 Atl. 774.

⁶⁵ *Alberta Rolling Mills Co. v. Christie*, 45 Dom. L. Rep. (Can.) 545, rev'g 38 Dom. L. Rep. 488.

⁶⁶ *Zapp v. Spreckels*, — Tex. Civ. App. —, 204 S. W. 786.

⁶⁷ *Zapp v. Spreckels*, — Tex. Civ. App. —, 204 S. W. 786.

⁶⁸ Construction of particular contracts, see *Cary v. Holt's Ex'rs*, 120 Va. 261, 91 S. E. 188.

Construction of agreement to subscribe balance of capital of stock, made by syndicate, see *Wing v. McCallum*, 244 Fed. 199.

⁶⁹ *Woldson v. Richmond Mining, Milling & Reducing Co.*, 102 Wash. 248, 172 Pac. 1162.

⁷⁰ *Mitchell v. Porter*, — Tex. —, 223 S. W. 197.

⁷¹ *Van Gilder v. Eagleson*, — Colo. —, 181 Pac. 539.

⁷² Liability to creditors for amount unpaid on subscription, see § 4095 et seq., *infra*.

⁷³ *Thomas v. Kalbfus*, 97 Ohio St. 232, 119 N. E. 412.

the laws of the state where the corporation is created and exists.⁷⁴

II. SUBSCRIPTIONS UPON EXPRESS CONDITIONS PRECEDENT, IMPLIED CONDITIONS PRECEDENT AND CONDITIONAL DELIVERY OF SUBSCRIPTIONS

§ 573. Conditional subscriptions defined. A condition precedent need not be expressly stated as such but it is sufficient that the conditions clearly are conditions precedent.⁷⁵

§ 574. Conditional subscriptions distinguished from subscriptions upon special terms.⁷⁶ A subscriber on a condition subsequent is nevertheless a stockholder,⁷⁷ and the conditions subsequent are no defense in an action by the corporation on a subscription.⁷⁸ Where a contract is made to sell property to a corporation, to be paid for by stock and money, payment by the corporation of stock and money was not a "condition" of the subscription, as that term is used in the law of conditional subscriptions.⁷⁹

§ 577. Oral conditions affecting written subscriptions.⁸⁰ Parol evidence ordinarily is not admissible to show that the written subscription was conditional⁸¹ or otherwise vary the subscription contract.⁸² For instance, parol evidence is not admissible to contradict a note given for stock by showing it was not to be paid unless from commissions for selling stock.⁸³

⁷⁴ *United States Cast Iron Pipe & Foundry Co. v. Henry Vogt Mach. Co.*, 182 Ky. 473, 206 S. W. 806.

⁷⁵ *Canyon Creek Elevator & Milling Co. v. Allison*, 53 Mont. 604, 165 Pac. 753.

⁷⁶ Distinction between conditional subscription and a subscription upon special terms restated in *Natwick v. Terwilliger*, 24 Wyo. 253, 160 Pac. 338.

⁷⁷ *Alberta Rolling Mills Co. v. Christie*, 45 Dom. L. Rep. (Can. 545, rev'g 38 Dom. L. Rep. 488.

⁷⁸ *Re Monarch Bank of Canada*, 48 Dom. L. Rep. (Can.) 588.

⁷⁹ *Wallace v. Weinstein*, 257 Fed. 625, 628.

⁸⁰ That condition must be in writing, see *Kramer v. Hamsher*, 63 Pa. Super. Ct. 211.

⁸¹ *Raleigh Improvement Co. v. Andrews*, 176 N. C. 280, 96 S. E. 1032.

Note on "Admissibility of parol evidence to show that subscription to stock was conditional," see *Ann Cas.* 1918 C 853.

⁸² See § 609, *infra*.

⁸³ *Denman v. Kaplan*, — Tex. Civ. App. —, 205 S. W. 739.

§ 579. **Effect of valid conditional subscriptions—Before performance or fulfillment of condition.** If the subscription is conditional, no recovery can be had on it if the condition is not performed.⁸⁴ If a condition precedent is never fulfilled, the subscriber is not liable even though the corporation has been formed.⁸⁵ If the subscription is conditional, the corporation cannot recover without showing performance of the condition.⁸⁶

§ 584. — **Right to withdraw conditional subscriptions.**⁸⁷

§ 587. **Implied conditions precedent—Formation of corporation and effect of irregularity or failure to incorporate—Subscriptions before corporation is formed.** Agreements to subscribe for the stock of a corporation to be formed presuppose the organization of the corporation before they become binding and enforceable.⁸⁸ If the proposed company never comes into existence, the amount paid on a subscription to stock must be returned.⁸⁹

§ 589. — **Power to issue stock subscribed for.** A subscriber may recover back the amount paid where the issue of stock was void as beyond the corporate powers.⁹⁰ Where stock was unlawfully issued, as distinguished from mere irregularity in the issuance, a stockholder may attack the issue and recover the money paid the corporation for his stock.⁹¹ A note given for stock after the capital stock has been fully subscribed by others is without consideration, since in such a case the corporation had no power to solicit additional subscriptions.⁹² Where preferred

⁸⁴ Seubert v. Scott, 39 S. D. 278, 164 N. W. 75.

⁸⁵ Canyon Creek Elevator & Milling Co. v. Allison, 53 Mont. 604, 165 Pac. 753.

⁸⁶ Louisville Trust Co. v. McCabe, 183 Ky. 801, 211 S. W. 435.

⁸⁷ Notice of withdrawal, necessity for in particular case, see Canyon Creek Elevator & Milling Co. v. Allison, 53 Mont. 604, 165 Pac. 753.

⁸⁸ Jermyn v. Searing, 225 N. Y. 525, 122 N. E. 706, aff'g 170 N. Y. App. Div. 707, 156 N. Y. Supp. 718.

⁸⁹ Lucero v. Colorado Life Ins. Co., — Colo. —, 184 Pac. 379.

⁹⁰ Heide v. Capital Securities Co., 200 Ala. 397, 76 So. 313.

⁹¹ Heide v. Capital Securities Co., 200 Ala. 397, 76 So. 313.

⁹² Morrill v. Harris, 23 N. M. 146, 167 Pac. 276.

stock is issued in a larger amount than is authorized by statute, a subscriber may recover back the amount paid by him.⁹³

§ 593. — Issue or tender of certificate of stock. A certificate of stock need not be issued to complete a subscription to stock.⁹⁴ But refusal of the corporation to issue stock to a subscriber after payment of the price on a second subscription warrants a refusal to pay instalments on an earlier subscription.⁹⁵ So where a corporation agrees to issue stock to a purchaser, it must do so within a reasonable time.⁹⁶ In an action by a subscriber against the corporation for breach of contract to deliver the stock, defendant cannot escape liability by tendering, at the trial, the stock, where it had in the meantime become worthless, since the measure of damages is the market value of the stock at the time of the breach of contract.⁹⁷

§ 598. Waiver of conditions by subscriber. Waiver is generally a question of fact,⁹⁸ but there is no waiver where there is lack of knowledge.⁹⁹ For instance, acceptance of stock subscribed for without knowledge that the balance of the stock had not been subscribed is not a waiver of such condition precedent.¹ An option to return stock subscribed for may be waived by agreeing to a reorganization.²

§ 599. Estoppel of subscriber.³

III. SUBSCRIPTIONS UPON SPECIAL TERMS

§ 602. Power to accept subscriptions upon special terms, and validity thereof—In general.⁴ Conditions imposed by a town

⁹³ Citizens' Loan & Savings Co. v. Arwood, — Ala. App. —, 81 So. 854.

⁹⁴ Majors v. Girdner, 31 Cal. App. 47, 159 Pac. 826.

⁹⁵ Texas Co-Operative Inv. Co. v. Clark, — Tex. Civ. App. —, 216 S. W. 220.

⁹⁶ Kirkpatrick v. Lebus, 184 Ky. 139, 211 S. W. 572, holding a year an unreasonable time.

⁹⁷ Mutual Loan Society v. Stowe, 15 Ala. App. 293, 73 So. 202.

⁹⁸ See Canyon Creek Elevator &

Milling Co. v. Allison, 53 Mont. 604, 165 Pac. 753; Natwick v. Terwilliger, 24 Wyo. 253, 160 Pac. 338.

⁹⁹ Stuart v. New York Community Mausoleum Const. Co., 190 N. Y. App. Div. 906, 179 N. Y. Supp. 73.

¹ Enterprise Sheet Metal Works v. Schendel, — Mont. —, 173 Pac. 1059.

² Moore v. States Auto Supply Co., 184 Iowa 984, 169 N. W. 322.

³ See § 4106, *infra*.

⁴ Construction of agreement to

meeting on subscription to stock by a town must be observed, in order to render the subscription enforceable.⁵ Where a subscription is based on conditions as to erection of buildings, etc., the subscriber is entitled to a refund if the conditions are not fulfilled.⁶ If stock is issued with a stipulation that the money paid shall be refunded on failure to move the general offices of the corporation to where the subscriber resides, the stipulation is a valid one and the remedy of the subscriber, on failure of the corporation to comply therewith, is to return the stock and demand a return of his money.⁷ If the subscription is made on an agreement that certain persons should not be interested in the corporation, the subscriber may rescind and recover back the money paid, on a breach thereof, although the promoters had no knowledge that such persons were interested.⁸

§ 603. — Violation of charter, statutory or constitutional provisions.⁹

§ 604. — Agreements for surrender or repurchase of stock. Agreements to repurchase stock sold are valid in most of the states.¹⁰ Thus, in Minnesota, where no rights of creditors are involved, a corporation may, on a sale of its stock, give a right of rescission or return.¹¹ So, in Pennsylvania, a corporation, on selling undisposed of stock remaining in the treasury, may promise to furnish a buyer for the stock within six months, if desired, at a price to net the purchaser a specified profit.¹² On

repay subscription out of first dividends declared, see *Leslie v. Ebner*, — Ind. App. —, 118 N. E. 829.

⁵ *Plymouth & S. St. R. Co. v. Inhabitants of Plymouth*, 231 Mass. 535, 121 N. E. 398.

⁶ *Christie v. Alberta Rolling Mills Co.*, 38 Dom. L. Rep. (Can.) 488.

⁷ *Gasser v. Great Northern Ins. Co.*, — Minn. —, 176 N. W. 484, holding, however, that stock salesman had no implied authority to make such an agreement.

⁸ *Lauer v. Raymond*, 190 N. Y. App. Div. 319, 180 N. Y. Supp. 31.

⁹ See § 568, *supra*.

¹⁰ If the subscriber has the option to cancel the subscription at the end of a year, and he exercises the option, the corporation must repay the money paid. *Swartz v. Burr*, — Cal. App. —, 185 Pac. 411.

¹¹ *Gasser v. Great Northern Ins. Co.*, — Minn. —, 176 N. W. 484, referring to Missouri and Tennessee cases as holding the contrary in those states.

¹² *Lemmon v. East Palestine Rubber Co.*, 260 Pa. 28, 103 Atl. 510.

the other hand, in Missouri, a corporation cannot agree with a subscriber to repurchase the stock for the sum paid therefor;¹³ and in Oregon an agreement to resell, where indirectly an agreement by the corporation to purchase its own stock, is ultra vires where the corporation has no power to purchase its own stock.¹⁴ In New Mexico it is held that unless power is conferred on the officers by charter or statute or by-laws, they have no power to agree with a subscriber that he may cancel his subscription at his option at any time before the maturity of his note given in payment for the stock and have his note returned, since such an agreement is contrary to public policy.¹⁵ In Canada it is held that a condition subsequent in a subscription by which under certain circumstances the subscriber may surrender his shares and demand a return of his money is beyond the power of the corporation as involving an unlawful reduction of capital.¹⁶

Of course if the agreement is to repurchase on or before a certain date, the subscriber cannot compel repayment five months after such date.¹⁷ Where a corporation agrees to repurchase stock sold an employee in case he quits or is discharged, the election is solely that of the employee and he cannot recover the amount agreed on until he elects to turn back the stock and actually tenders it.¹⁸ Failure to exercise the option to compel a repurchase of stock within a reasonable time (in this case four and a half years), where no time is provided for its exercise, raises a presumption of abandonment of the option.¹⁹ A subscriber cannot rescind his subscription where he was authorized to if not satisfied after a visit to the plant, where he made no visit to the plant.²⁰

Where stock was sold by a company on a certain condition on failure of which the money paid was to be refunded, the

¹³ *Interstate Grocer Co. v. Taylor*, 200 Mo. App. 205, 204 S. W. 408.

¹⁴ *Fogarty v. Hunter*, 83 Ore. 183, 162 Pac. 964.

¹⁵ *Morrill v. Mastin*, 23 N. M. 563, 170 Pac. 45.

¹⁶ *Alberta Rolling Mills Co. v. Christie*, 45 Dom. L. Rep. (Can). 545, rev'g 38 Dom. L. Rep. 488.

¹⁷ *Gallant v. Credit Foncier Ca-*

nadien, — R. I. —, 103 Atl. 701.

¹⁸ *Security Sav. Bank v. Workman*, — Iowa —, 176 N. W. 307.

¹⁹ *Hertzler v. Federal Equipment Co.*, 265 Pa. 449, 109 Atl. 152, citing 2 *Fletcher Cyc. Corp.* p. 1322.

²⁰ *Murphy v. National Rubber Co. of New York*, 170 N. Y. Supp. 42.

remedy on failure of the condition was not an action to recover damages but instead an exercise of the option to return the stock and demand a return of the money.²¹ Where a part of the consideration for subscribing to stock was an agreement to furnish the subscriber with a buyer for the stock within six months at a profit, and the contract was entire and indivisible, the failure to furnish such a buyer makes the corporation liable to the subscriber.²²

§ 606. — Subscriptions constituting a fraud upon other stockholders or creditors—In general. Secret agreements generally are discharged by law although they may be enforceable against the promoters who make them.²³

§ 607. — — Agreements for surrender or repurchase of stock. The agreements referred to in section 604 will not be upheld if a fraud on other subscribers nor where the rights of corporate creditors are affected, and hence the agreement cannot be enforced after insolvency of the corporation.²⁴ Conceding that the agreement to repurchase is unenforceable when the corporation is insolvent, the stockholder cannot recover on the theory that there is a failure of consideration and that it would be unfair to permit the corporation to retain the purchase price of the stock; and it is immaterial that the corporation was insolvent at the time the contract was made.²⁵

§ 608. — Authority of agents receiving subscriptions. A corporate agent selling stock has ostensible authority to agree that the company will buy it back in ten months if the subscriber is not satisfied.²⁶ It has been held that the corporation is liable for the act of its selling agent within his apparent authority in agreeing that the company would buy back the stock within ten months at the price paid, although he merely indorsed such agreement on the duplicate subscription and not

²¹ Gasser v. Great Northern Ins. Co., — Minn. —, 176 N. W. 484.

²² Lemmon v. East Palestine Rubber Co., 260 Pa. 28, 103 Atl. 510.

²³ Raich v. Lindebek, 36 N. D. 133, 161 N. W. 1026.

²⁴ Hoover Steel Ball Co. v.

Schaefer Ball Bearings Co., 90 N. J. Eq. 164, 106 Atl. 471.

²⁵ Hoover Steel Ball Co. v. Schaefer Ball Bearings Co., 90 N. J. Eq. 164, 106 Atl. 471.

²⁶ Tidewater Southern R. Co. v. Harney, 32 Cal. App. 253, 162 Pac.

664.

on the original turned into the company.²⁷ In another state, where an agent, in selling stock, agreed with the subscriber to resell the stock within a certain time for the subscriber's benefit, which he did not do, the subscriber cannot compel the corporation to refund the amount paid. There is no false representation such as to constitute fraud and no consideration for the agreement to refund.²⁸

A corporation ratifies the act of a stock salesman in agreeing to refund money paid for stock on failure of the company to move its office, by delivering the stock with knowledge of such condition and by claiming the benefit of the subscription.²⁹

§ 609. — Oral stipulations—Other writings.³⁰ Where a subscription contract is reduced to writing and signed, all oral agreements, whether prior or contemporaneous, are merged in it, and parol evidence of them cannot be received to vary the legal purport of the writing.³¹ An agreement of an officer selling stock for the corporation to himself repurchase it in case of dissatisfaction need not be in writing.³²

IV. FRAUD IN PROCURING SUBSCRIPTIONS

§ 610. Effect of fraud in general.³³ Fraud authorizes subscribers to avoid their subscriptions.³⁴ A subscriber to stock may rescind his contract of subscription where induced by fraud of a promoter, notwithstanding the fraud was committed before the corporation was formed, where the contract of subscription was made for the benefit of the corporation and it accepted the benefits thereof.³⁵

²⁷ *Tidewater Southern R. Co. v. Harney*, 32 Cal. App. 253, 162 Pac. 664, and see *Tidewater Southern R. Co. v. Vance*, 31 Cal. App. 503, 160 Pac. 1097.

²⁸ *Meixner v. Western Live Stock Ins. Co.*, 203 Ill. App. 523.

²⁹ *Gasser v. Great Northern Ins. Co.*, — Minn. —, 176 N. W. 484.

³⁰ See also §§ 569, 577, *supra*.

³¹ *Raleigh Improvement Co. v. Andrews*, 176 N. C. 280, 96 S. E. 1032.

³² *Lingelbach v. Luckenbach*, 168 Wis. 481, 170 N. W. 711.

³³ Effect of fraud, and what constitutes, where stock is sold by a stockholder to a third person, see § 3862 et seq., *infra*.

³⁴ *Lone Star Life Ins. Co. v. Pierce*, — Tex. Civ. App. —, 200 S. W. 1104; *Vancouver Life Ins. Co. v. Richards*, 48 Dom. L. Rep. (Can.) 707.

³⁵ *Stone v. Walker*, 201 Ala. 130, L. R. A. 1918 C 839, 77 So. 554, a leading case.

§ 611. Want of authority on part of person making representation. A corporation accepting a subscription to its stock procured by one technically not its agent, through fraudulent representations made without its authority, becomes responsible for the fraud.³⁶ Fraudulent representations of promoters in obtaining subscriptions to stock are binding on the corporation afterwards formed and which adopted such subscriptions.³⁷

The case of *Jones v. Bankers' Trust Co.*, 235 Fed. 649, cited in volume 2 as supporting the proposition that provisions in the contract that no representations made by the person taking the subscription shall be binding on the company, unless embodied in the written contract, prevents a rescission for false representations not embodied in the contract, was reversed on rehearing in 239 Fed. 770, on the ground that the provision in the contract was that no "statement, representation or agreement of warranty" should be binding unless reduced to writing, and hence that it applied only to warranties so that oral representations not warranties were binding although not embodied in the contract. It was also held that under the rule that "where one party to a trade has been induced to enter it through the fraud, deceit, and misrepresentations of the other party, in material matters, no binding trade results, and the defrauded party does not become bound by its terms," fraud in securing the subscription may be shown as a defense regardless of the terms of the written contract.³⁸

§ 612. What amounts to fraud in procuring subscriptions—
In general. What amounts to fraud in procuring a subscription to stock is governed by the rules governing fraud in relation to contracts in general.³⁹ The fraud must be clearly

³⁶ *Cator v. Commonwealth Bonding & Casualty Ins. Co.*, — Tex. —, 216 S. W. 140.

The fact that the misrepresentation was unauthorized and not known by the corporation itself is immaterial. *Rhoades v. Banking, Trust & Mortgage Co.*, 125 Va. 320, 99 S. E. 673.

³⁷ *Stone v. Walker*, 201 Ala. 130, L. R. A. 1918 C 839, 77 So. 554.

³⁸ *Jones v. Bankers' Trust Co.*, 239 Fed. 770.

³⁹ Facts in particular cases as showing fraud, see *Romunder v. Caskey*, 137 Ark. 574, 209 S. W. 735; *Burns v. Bauer*, 37 Cal. App. 251, 174 Pac. 346; *Planters' Bank of Yatesville v. Brown*, 22 Ga. App. 495, 96 S. E. 328; *Leslie v. Ebner*, — Ind. App. —, 118 N. E. 829; *Sherman v. Smith*, 185 Iowa 654, 169 N. W. 216; *Lindsay*

shown.⁴⁰ Circulars sent out by the corporation to prospective purchasers of stock are admissible to show fraud.⁴¹ On an issue as to misrepresentations as to value of stock sold by the corporation, it being represented that it was worth par, evidence is admissible of a statement by the president two years later that the stock at the time of the sale was worth only forty cents on the dollar.⁴²

§ 614. — Representations as to financial conditions. The fraudulent representations may relate to the financial condition of the company.⁴³

§ 615. — Representations as to capital stock. A positive statement that certain persons were to take stock in the proposed corporation and pay for such stock in cash, where known to be false, is such fraud as to warrant a rescission.⁴⁴ Misrepresentation that stock is nonassessable is one of fact so as to be a defense to an action on the subscription.⁴⁵ Misrepresentations of existing facts as to amount of stock subscribed, that business had been commenced, and that several wealthy and influential men had subscribed ten thousand dollars worth of stock, are fraudulent.⁴⁶ False representations that promoters had no interest in certain options but were subscribers on the same basis as others, where an inducement to the subscription, are ground for rescission.⁴⁷ Fraudulent misrepresentations as to listing of the stock on the Stock Exchange are ground for rescission.⁴⁸

v. Sonora Gold Mining & Milling Co., — Mo., 196 S. W. 764.

⁴⁰ Western Casualty & Guaranty Ins. Co. v. McLean, — Okla., 181 Pac. 494; Rhoades v. Banking, Trust & Mortgage Co., 125 Va. 320, 99 S. E. 673.

⁴¹ Mangold & Glandt Bank v. Utterback, — Okla., 174 Pac. 542.

⁴² Rosenberger v. H. E. Wilcox Motor Co., — Minn., 177 N. W. 625, citing 3 Fletcher Cyc. Corp. § 2160.

⁴³ See Biel v. Union Fuel & Ice Co., 105 Wash. 41, 177 Pac. 813, holding certain evidence admissible.

⁴⁴ Ritzwoller v. Lurie, 225 N. Y. 464, 122 N. E. 634, modifying 180 N. Y. App. Div. 934, 167 N. Y. Supp. 1123.

⁴⁵ Merchants' Realty & Investment Co. v. Kelso, — Cal. App., 189 Pac. 116.

⁴⁶ Maginess v. Western Securities Corporation, 38 Cal. App. 56, 175 Pac. 277.

⁴⁷ Munson v. Fishburn, — Cal., 190 Pac. 808.

⁴⁸ Sarantides v. Williams, Belmont & Co., — N. Y. App. Div., 180 N. Y. Supp. 741.

§ 616. — Representations as to dividends. Representations as to the returns from stock, although in the nature of an opinion and of a promissory character, are actionable in some states.⁴⁹

§ 617. — Further illustrations. It is a fraud to falsely represent that the company would be ready for business within two months,⁵⁰ or that another person on whose business capacity much reliance was placed had advised subscribing to the stock.⁵¹ Fraudulent representations as to the nature of the paper signed, where relied upon, are ground for rescission.⁵²

§ 618. — Expression of opinion or prediction. Generally mere statements of opinion are not actionable fraud,⁵³ although in some states misrepresentations are actionable even though partaking of the nature of opinion and of a promissory character.⁵⁴

Statements as to the future prospects of the business are matters of opinion,⁵⁵ as is a statement that the gate receipts of the first ball game of the season would be sufficient to meet the financial requirements of a baseball club.⁵⁶ Representations as to the financial condition of the company, the volume of its business, the amount of its income and expenses, the value of its stock, and its immediate financial prospects, are all matters of fact and not expressions of opinion, and if false are actionable fraud.⁵⁷

⁴⁹ Texas Co-Operative Inv. Co. v. Clark, — Tex. Civ. App. —, 216 S. W. 220.

⁵⁰ Buhler v. Loftus, 53 Mont. 546, 165 Pac. 601.

⁵¹ Vulcan Fire Ins. Co. v. Jorgensen, 33 Cal. App. 763, 166 Pac. 835.

⁵² Raich v. Lindbek, 36 N. D. 133, 161 N. W. 1026.

⁵³ Citizens' State Bank of Roundup v. Snelling, — Mont. —, 178 Pac. 744; Philadelphia Motor Speedway Ass'n v. Sale, 69 Pa. Super. Ct. 583; Burchill v. Hermes-meyer, — Tex. Civ. App. —, 212 S. W. 767; Rhoades v. Banking, Trust & Mortgage Co., 125 Va. 320, 99 S. E. 673.

Representations as to value as fraud, see Palmer v. Citizens' Bank of Murray, 179 Ky. 54, 200 S. W. 41.

⁵⁴ See Texas Co-Operative Ins. Co. v. Clark, — Tex. Civ. App. —, 216 S. W. 220.

⁵⁵ Bank of Valley City v. Lee, — N. D. —, 175 N. W. 575.

⁵⁶ Bucher v. Federal Baseball Club of Baltimore, 130 Md. 635, 101 Atl. 534, involving the Baltimore club of the defunct Federal League.

⁵⁷ Hood v. Wood, 61 Okla. 294, 161 Pac. 210.

§ 619. — **Promises and statements of intention.** Representations must relate to a past or existing fact rather than the future,⁵⁸ but a representation with reference to the future may be so related to present existent conditions that its affirmation as a fact will constitute a fraudulent representation.⁵⁹

§ 623. — **Knowledge of falsity and intention to deceive.** False representations, to be actionable, must have been made with an intent to deceive.⁶⁰ Knowledge of the falsity of the representations is not essential, but it is sufficient that those making them ought to have known that they were false.⁶¹ Knowledge of the fraud of its agent by the corporation is not necessary where it has accepted the subscription.⁶²

§ 625. — **Right to rely on representations.** Ordinarily a subscriber has a right to rely on representations.⁶³ A purchaser of stock may rely on representations of corporate agents acting apparently within the scope of their authority.⁶⁴

§ 626. — **Necessity for injury.** Injury as a result of the misrepresentations must be proved.⁶⁵ The complaint, in an action to rescind a subscription because of fraud, must show that damages have resulted to plaintiff.⁶⁶

On the question whether a subscriber sustained any injury from representations made by the agent as to the meritorious

⁵⁸ Wickwire v. Warner, 174 N. Y. Supp. 811; McCoy v. Bankers' Trust Co., — Tex. Civ. App. —, 200 S. W. 1138.

⁵⁹ Buhler v. Loftus, 53 Mont. 546, 165 Pac. 601.

⁶⁰ Burchill v. Hermsmeyer, — Tex. Civ. App. —, 212 S. W. 767.

⁶¹ Denis v. Nu-Way Puncture Cure Co., 170 Wis. 333, 175 N. W. 95.

⁶² Lone Star Life Ins. Co. v. Pierce, — Tex. Civ. App. —, 200 S. W. 1104.

⁶³ Mangold & Glandt Bank v. Utterback, — Okla. —, 174 Pac. 542. Compare, however, Citizens'

State Bank of Roundup v. Snelling, — Mont. —, 178 Pac. 744.

⁶⁴ Bankers' Trust Co. v. Calhoun, — Tex. Civ. App. —, 209 S. W. 826.

⁶⁵ Denis v. Nu-Way Puncture Cure Co., 170 Wis. 333, 175 N. W. 95.

In California, allegation or proof of pecuniary damage is not necessary. Vulcan Fire Ins. Co. v. Jorgensen, 33 Cal. App. 763, 166 Pac. 835.

⁶⁶ Ritzwoller v. Lurie, 176 N. Y. App. Div. 100, 162 N. Y. Supp. 175.

quality of the article to be produced by the corporation, it is proper to show that the company had gone out of business.⁶⁷

§ 627. Remedies of subscriber or purchaser in case of fraud—Rescission in general.⁶⁸ The remedy of the defrauded subscriber is either to (1) restore the original situation, rescind the contract, and recover back his money, or (2) offer to restore, and, by keeping such offer good, sue in equity for a rescission of the contract and for a recovery of the amount paid, or (3) sue the agent or the company, or both of them, at law for the damages resulting from the fraud.⁶⁹ The defrauded subscriber may sue the corporation in equity to rescind the sale or may plead the fraud as a defense to a suit for unpaid stock subscriptions.⁷⁰

Fraud may be set up as a defense in an action on the subscription,⁷¹ but there must be a rescission to entitle defendant to defend on the ground of fraud.⁷² If a note is given and transferred to a third person, then it seems the question whether he is a holder in due course is material in determining whether the defense of fraud can be interposed.⁷³

Another remedy is to sue in equity to cancel a mortgage and notes given in purchase of the stock.⁷⁴

The reasons for rescinding need not be stated in detail in the notice of rescission.⁷⁵

The bill in a suit to rescind a subscription for fraud must be

⁶⁷ *Denis v. Nu-Way Puncture Cure Co.*, 170 Wis. 333, 175 N. W. 95.

⁶⁸ General statement as to remedies, see *Tidewater Southern R. Co. v. Harney*, 32 Cal. App. 253, 162 Pac. 664.

⁶⁹ *Denis v. Nu-Way Puncture Cure Co.*, 170 Wis. 333, 175 N. W. 95.

Bringing of suit may constitute a sufficient rescission. *Mutual Loan Society v. Letson*, 200 Ala. 251, 76 So. 17.

⁷⁰ *Romunder v. Caskey*, 137 Ark. 574, 209 S. W. 735.

⁷¹ *Appalachian Corporation v. Ayo*, 145 La. 201, 82 So. 89.

In an action at law in the federal courts, on a stock subscription, the defense that the subscription was obtained by fraud, even though an equitable defense, may be set up. *Columbia-Knick-erbocker Trust Co. v. Abbot*, 247 Fed. 833.

⁷² *Independent Harvester Co. v. Lee*, 40 S. D. 472, 168 N. W. 28.

⁷³ *Appalachian Corporation v. Ayo*, 145 La. 201, 82 So. 89.

⁷⁴ *Buhler v. Loftus*, 53 Mont. 546, 165 Pac. 601.

⁷⁵ *Vulcan Fire Ins. Co. v. Jorgensen*, 33 Cal. App. 763, 166 Pac. 835.

clear and definite as to the fraud and other necessary allegations.⁷⁶

Where fraud or illegality inheres in a stock subscription contract, the fact may be shown by parol.⁷⁷

§ 628. — Recovery of money or other consideration paid.

The right to recover from the corporation the amount paid, on rescinding for fraud, is not barred by efforts to secure redress from the agent who made the sale.⁷⁸

The individual inducing the subscription is not a necessary or proper party to an action to rescind.⁷⁹ In Georgia, however, it is held that the corporation and its officers who participated in the fraud are proper parties to a suit in equity by a subscriber to rescind his subscription for fraud.⁸⁰

§ 629. — Action for deceit.⁸¹ The officer making the sale by fraudulent representations is liable jointly and severally with the corporation, in an action to recover damages.⁸²

§ 631. Limitations upon the right to rescind—Restoration of the status quo. In order to rescind a subscription, it is necessary to return the certificate and any dividends received,⁸³ but there is some conflict as to the necessity of returning stock which is of no value.⁸⁴ The other party must be put in statu quo.⁸⁵ There is nothing to return where no stock nor money has been received by the subscriber,⁸⁶ although it has been held

⁷⁶ Drennen v. Cooper, 200 Ala. 328, 76 So. 94.

⁷⁷ Ennis v. New World Life Ins. Co., 97 Wash. 122, 165 Pac. 1091.

⁷⁸ Denis v. Nu-Way Puncture Cure Co., 170 Wis. 333, 175 N. W. 95.

⁷⁹ Ritzwoller v. Lurie, 225 N. Y. 464, 122 N. E. 634, modifying 180 N. Y. App. Div. 934, 167 N. Y. Supp. 1123.

⁸⁰ American Nat. Bank v. Armstrong, 145 Ga. 618, 89 S. E. 691.

⁸¹ See Dunaway v. Stocks, 19 Ga. App. 267, 91 S. E. 345.

⁸² Denis v. Nu-Way Puncture Cure Co., 170 Wis. 333, 175 N. W. 95.

⁸³ Mutual Loan Co. v. Letson, 202 Ala. 683, 81 So. 659.

⁸⁴ See Cator v. Commonwealth Bonding & Casualty Ins. Co., — Tex. —, 216 S. W. 140.

⁸⁵ Cator v. Commonwealth Bonding & Casualty Ins. Co., — Tex. —, 216 S. W. 140.

⁸⁶ Vulcan Fire Ins. Co. v. Jorgensen, 33 Cal. App. 763, 166 Pac. 835.

that the subscriber must return or offer to return the stock even if the certificate was never delivered to him.⁸⁷

§ 633. — **Ratification or waiver as a bar to rescission.**⁸⁸ Demanding dividends over a year after the purchase waives the right to rescind,⁸⁹ as does retention of the certificate of stock and receipt and retention of several dividends after knowledge of the fraud,⁹⁰ or treating the stock as one's own and attempting to sell it after knowledge of the fraud.⁹¹ So there is a waiver of the right to rescind where the subscriber attempts to sell the stock and participates as an officer in managing the business.⁹² A fortiori, a transfer of his stock by a subscriber after knowledge of a ground for cancellation of his subscription is a waiver of the right to cancel on that ground.⁹³ But acts done before knowledge of the fraud do not constitute a ratification.⁹⁴ Thus, transfer of his stock by a subscriber is not a waiver of fraud of which he has no knowledge.⁹⁵ So the unauthorized acts of another, not within the scope of his actual or apparent authority as proxy or as attorney, are not binding on subscribers to stock as a ratification.⁹⁶

Of course a subscriber cannot rescind where he has sold the stock back to the agent who committed the fraud.⁹⁷

§ 634. — **Laches as a bar to rescission.** Laches bars the right to rescind for fraud especially where the corporation is insolvent.⁹⁸ A delay of five weeks after the filing of a petition

⁸⁷ *Majors v. Girdner*, 31 Cal. App. 47, 159 Pac. 826.

⁸⁸ Executing proxy as waiver, see *Edward v. Ioor*, 205 Mich. 617, 172 N. W. 620.

⁸⁹ *Biel v. Union Fuel & Ice Co.*, 105 Wash. 41, 177 Pac. 813.

⁹⁰ *Corporation Funding & Finance Co. v. Stoffregen*, 264 Pa. 215, 107 Atl. 727.

⁹¹ *Independent Harvester Co. v. Lee*, 40 S. D. 472, 168 N. W. 28.

⁹² *Davis v. Gifford*, 182 N. Y. App. Div. 99, 169 N. Y. Supp. 492.

⁹³ *Cator v. Commonwealth Bonding & Casualty Ins. Co.*, — Tex. —, 216 S. W. 140.

⁹⁴ *Rhoades v. Banking, Trust & Mortgage Co.*, 125 Va. 320, 99 S. E. 673.

⁹⁵ *Cator v. Commonwealth Bonding & Casualty Ins. Co.*, — Tex. —, 216 S. W. 140.

⁹⁶ *Rhoades v. Banking, Trust & Mortgage Co.*, 125 Va. 320, 99 S. E. 673.

⁹⁷ See *Denis v. Nu-Way Puncture Cure Co.*, 170 Wis. 333, 175 N. W. 95.

⁹⁸ *Preston v. Jeffers*, 179 Ky. 384, 200 S. W. 654; *Robert v. Montreal Trust Co.*, 41 Dom. L. Rep. (Can.) 173.

for the appointment of a receiver was held not laches.⁹⁹ Delays of over six months,¹ a year,² or of two years³ or more,⁴ have been held fatal.

§ 636. — Effect of insolvency of the corporation. There is considerable conflict as to the right to rescind a stock subscription after the corporation has become insolvent. In a federal court it was held that a purchaser of stock in a national bank may rescind his purchase for fraud even after the appointment of a receiver.⁵ In Alabama, insolvency of the corporation does not necessarily bar the right to rescind a stock subscription for fraud.⁶ In Colorado, the right of a subscriber to rescind for fraud is inferior to the rights of creditors who became such after the subscription, where the corporation is insolvent.⁷ In Georgia, by statute, a subscriber cannot set up fraud after insolvency,⁸ and this was the rule in that state independent of statute so far as creditors who became such after the subscription are concerned.⁹

In Iowa it is held that if a subscriber acts diligently in discovering the fraud and repudiating the obligation as soon as the fraud is discovered, and there is no showing that there are creditors whose claims have accrued since the subscription, the rights of the subscriber to rescind are not barred by the insolvency of the company.¹⁰

⁹⁹ *Independent Van & Storage Co. v. Iowa Mercantile Co.*, 184 Iowa 154, 168 N. W. 782.

¹ Laches for over six months after receiving stock held a bar to rescission in *Sarantides v. Williams, Belmont & Co.*, — N. Y. App. Div. —, 180 N. Y. Supp. 741; — N. Y. Misc. —, 184 N. Y. Supp. 612.

² Silence for more than a year after notice precludes attack on a subscription for fraud or illegality. *Montreal Trust Co. v. Robert*, 36 Dom. L. Rep. (Can.) 516.

³ *Van Gilder v. Eagleson*, — Colo. —, 181 Pac. 539; *Preston v. Jeffers*, 179 Ky. 384, 200 S. W. 654.

⁴ *Lucero v. Colorado Life Ins.*

Co., — Colo. —, 184 Pac. 379; *Van Gilder v. Eagleson*, — Colo. —, 181 Pac. 539.

⁵ *Salter v. Williams*, 244 Fed. 126.

⁶ *Stone v. Walker*, 201 Ala. 130, L. R. A. 1918 C 839, 77 So. 554.

⁷ *Van Gilder v. Eagleson*, — Colo. —, 181 Pac. 539, following the English rule.

⁸ *Wright v. Hix*, — Ala. —, 83 So. 341.

⁹ *Cosmopolitan Life Ins. Co. v. Sheats*, 20 Ga. App. 622, 93 S. E. 507.

¹⁰ *Independent Van & Storage Co. v. Iowa Mercantile Co.*, 184 Iowa 154, 168 N. W. 782, where receivership was within sixty days after subscription and stockholder

The Kentucky rule as to the right to rescind a subscription for fraud after insolvency of the corporation is that a rescission is proper if the subscriber "derived no benefit from his purchase of the stock, and did not discover, and by the exercise of the utmost care could not have discovered, the fraud before the bank or corporation became insolvent."¹¹ In that state, fraud is no defense where a receiver sues for the subscription price, except where the stockholder acquired his stock so short a time before the insolvency of the corporation that he had no reasonable opportunity to investigate.¹²

In Texas it is said that "it is a general rule that, in a suit to collect such unpaid subscription, it is no valid defense that the subscription contract was procured by fraudulent misrepresentations."¹³ In that state, a subscriber may obtain the cancellation of his subscription contract for fraud although the corporation became insolvent after the suit was brought, where none of the creditors represented by the receiver became creditors after plaintiff's subscription nor were induced by such subscription to extend credit to the corporation.¹⁴

In Canada, a subscription cannot be repudiated after a reasonable time where the rights of creditors have intervened, as by a winding-up order.¹⁵

V. WITHDRAWAL, RELEASE AND DISCHARGE OF SUBSCRIBERS

§ 637. Withdrawal of subscribers. A subscriber cannot recover money paid while he holds the certificate of stock and retains money received as dividends.¹⁶

intervened within five weeks thereafter.

Fraud is no defense to an action on a subscription to stock, it is held in Iowa, where the action is brought by the receiver after insolvency and it is shown "that there are claims in the hands of the receiver to be satisfied out of the corporate assets, that accrued after the subscriber had obligated himself as a stockholder." *Lamb v. Bonesteel*, — Iowa —, 173 N. W. 13, following *Independent Van & Storage Co. v. Iowa Mercantile Co.*, 184 Iowa 154, 168 N. W. 782.

¹¹ *Smith v. Jones*, 173 Ky. 776, L. R. A. 1917 C 890, 191 S. W. 500.

¹² *Levassor v. Metropolitan Fire Ins. Co.'s Receiver*, 188 Ky. 23, 220 S. W. 752.

¹³ *Mitchell v. Porter*, — Tex. Civ. App. —, 194 S. W. 981.

¹⁴ *Mitchell v. Hancock*, — Tex. Civ. App. —, 196 S. W. 694.

Texas rule reiterated in *Thompson v. First State Bank*, — Tex. Civ. App. —, 189 S. W. 116.

¹⁵ *Barrett v. Bank of Vancouver*, 36 Dom. L. Rep. (Can.) 158.

¹⁶ *Mutual Loan Society v. Let-*

§ 638. Release of subscribers by the corporation—Right of corporation or its officers in general.¹⁷ A subscriber to stock may be released by the corporation with the consent of all the other subscribers, if the rights of creditors are not involved,¹⁸ provided there is a consideration for the release. There is no consideration for a cancellation of a subscription merely because the subscriber had advanced money for the benefit of the corporation and had indorsed a note made by it for rent.¹⁹ The doctrine that “subscribed, but unpaid, capital stock of a corporation becomes, upon its insolvency and suspension of business, a trust fund for all creditors, and that, even before insolvency, it so far has that inchoate character as to prevent it from being surrendered or given away by the corporation, finds universal acceptance.”²⁰ A corporation “may, under certain circumstances, and certainly as against all but existing creditors, cancel a subscription to stock, especially if the cancellation relate to only a part of the shares subscribed for.”²¹

Corporate directors or officers have no inherent power to cancel stock subscriptions.²² Neither the directors nor the officers of a corporation can cancel a subscription without the consent of all the stockholders unless the power to do so has been granted by the charter or governing statute.²³ Promoters cannot relieve unconditional subscribers from their subscription without the consent of the other subscribers.²⁴

§ 639. — Right as against creditors or dissenting stockholders.²⁵ An agreement to release a subscriber, even if based

son, 202 Ala. 683, 81 So. 659, and see § 631, *supra*.

¹⁷ Cancellation of agreement to subscribe as distinguished from cancellation of actual subscription, see *Murphy v. Pantan*, 96 Wash. 637, 165 Pac. 1074.

¹⁸ *Murphy v. Pantan*, 96 Wash. 637, 165 Pac. 1074.

¹⁹ *Murphy v. Pantan*, 96 Wash. 637, 165 Pac. 1074.

²⁰ *Thomas & Brenneman v. Goodman*, 254 Fed. 39, 41.

²¹ *Pasadena Rapid Transit Co. v. Munson*, 37 Cal. App. 352, 174 Pac. 109.

²² *Morrill v. Harris*, 23 N. M. 146, 167 Pac. 276.

²³ *Mutual Loan Society v. Letson*, 202 Ala. 683, 81 So. 659.

Directors or other officers have no power, unless expressly conferred, to agree with a subscriber that his subscription shall be canceled and his note returned. *Morrill v. Harris*, 23 N. M. 146, 167 Pac. 276.

²⁴ *Leroy v. Davis & Co.*, 46 Dom. L. Rep. (Can.) 568.

²⁵ See also § 4104, *infra*.

on a consideration, is not binding as against creditors who would be injured thereby.²⁶ A compromise with a subscriber to stock, after acceptance of the subscription, is binding on other stockholders where in good faith and for a valuable consideration.²⁷

§ 640. — Exceptions to and modifications of the rule. If a subscriber is insolvent, the corporation may compromise its claim for the amount due if there is a valuable consideration.²⁸

§ 642. Discharge by payment.²⁹ The subscriber cannot credit himself with sums paid on another subscription.³⁰

§ 644. Discharge in bankruptcy. A stockholder's discharge in bankruptcy, after insolvency of the corporation, relieves him of his statutory liability for debts of the company.³¹

§ 646. Discharge by nonperformance of conditions precedent or special terms.³² Failure to issue a certificate of stock does not release a subscriber.³³ On breach of a condition to the purchase of stock in a corporation to be formed, that certain persons should not be interested in the corporation, the purchaser is entitled to rescind and recover back the money paid.³⁴

§ 647. Discharge by alteration or amendment of charter.³⁵ An agreement to purchase 5 shares of stock of a par value of \$100, there being 40,000 shares and the capital stock consisting of \$4,000,000, is not enforceable by the corporation after it reduces its stock to \$400,000 consisting of 40,000 shares of a par value of \$10.³⁶ Where a subscription was made to 5 shares

²⁶ Preston v. Jeffers, 179 Ky. 384, 200 S. W. 654.

²⁷ Martin v. Cushwa, — W. Va. —, 104 S. E. 97.

²⁸ Murphy v. Pantou, 96 Wash. 637, 165 Pac. 1074.

²⁹ See also § 712, *infra*.

³⁰ Vaughan-Robertson Drug Co. v. Grimes-Mills Drug Co., 173 N. C. 502, 92 S. E. 376.

³¹ See § 4265, *infra*.

³² See also §§ 602, 608, *supra*.

³³ Preston v. Jeffers, 179 Ky. 384, 200 S. W. 654.

³⁴ Lauer v. Raymond, 190 N. Y. App. Div. 319, 180 N. Y. Supp. 31.

³⁵ See also § 524, *supra*.

Note on "Alteration in charter or change in corporate design as releasing subscriber to stock," see Ann. Cas. 1918 A 79.

³⁶ Campbell v. Coin Mach. Mfg. Co., — Ore. —, 188 Pac. 197.

of stock whose par value was \$100 a share, and part of the price was paid, the subscriber may recover it back where the corporation, before the last instalment was due, reduced the par value of shares to \$10.³⁷

§ 650. Special agreements with, release or withdrawal of, or nonpayment by, other subscribers. Improper release of other subscribers does not release a subscriber;³⁸ and an attempted release of another shareholder from his stock subscription, where such release is void, is no defense.³⁹

§ 652. Mismanagement of the corporation, illegal election of officers, etc. Mismanagement of the corporate officers does not release a subscriber,⁴⁰ nor does waste of assets by the corporate officers.⁴¹

§ 654. Nonuser or abandonment of enterprise. A mere abandonment of the corporate enterprise is not necessarily a good defense to an action on a subscription;⁴² and the mere fact that work on the corporate undertaking has been suspended is not such an abandonment of the enterprise as will discharge a subscriber.⁴³ So mere failure of the corporation venture is not a failure of consideration for a note given in exchange for stock,⁴⁴ although in Texas it has been held that where the corporation was solvent and owed nothing but had sold all its assets and abandoned business, a stock subscription note is not collectible because of failure of consideration.⁴⁵ It is no ground for canceling a stock subscription that the company has not been a success where due to want of sufficient working capital.⁴⁶

³⁷ Lane v. Coin Machine Mfg. Co., 69 Pa. Super. Ct. 373.

³⁸ Preston v. Jeffers, 179 Ky. 384, 200 S. W. 654.

³⁹ Hauger v. International Trading Co., 184 Ky. 794, 214 S. W. 438.

⁴⁰ Preston v. Jeffers, 179 Ky. 384, 200 S. W. 654.

⁴¹ Preston v. Jeffers, 179 Ky. 384, 200 S. W. 654.

⁴² Raleigh Improvement Co. v.

Andrews, 176 N. C. 280, 96 S. E. 1032.

⁴³ Raleigh Improvement Co. v. Andrews, 176 N. C. 280, 96 S. E. 1032.

⁴⁴ Bank of Valley City v. Lee, — N. D. —, 175 N. W. 575.

⁴⁵ Shield v. Lone Star Life Ins. Co., — Tex. Civ. App. —, 202 S. W. 211.

⁴⁶ Shaw v. Carr, 93 Wash. 550, 161 Pac. 345.

The principle that nonuser of a corporate franchise will not release a subscriber ought not to be applied where unreasonable.⁴⁷ For instance, where money is not required by a corporation for any corporate purpose for the reason that it has ceased doing business and has no debts, and where it cannot be determined what proportion of an unpaid subscription is required to pay such subscriber's share of the losses sustained by the corporation, a claim for the unpaid balance of his subscription cannot be collected in a probate court.⁴⁸

§ 656. Statute of limitations.⁴⁹ The Ohio statute limiting the time to sue to enforce the secondary or double liability of stockholders for corporate debts to eighteen months does not apply to actions to recover the balance due on stock subscriptions.⁵⁰

Instalments on subscriptions to stock may be postponed as to time of payment, by acts of the directors ratified by the stockholders, so as to change the time when the cause of action accrues within the statute of limitations.⁵¹

VI. REMEDIES OF CORPORATION AGAINST SUBSCRIBERS

§ 657. Actions on subscriptions—In general.⁵² Where a subscription is made before incorporation, the corporation when created may sue thereon.⁵³ The action need not be authorized by a formal resolution of the directors.⁵⁴ There is an implied promise to pay the par value of stock issued to and accepted by a subscriber.⁵⁵ There is no liability, under ordinary circumstances, where stock fully paid is transferred to the corporation and an agreement made to subscribe for the same amount

⁴⁷ *Wicks Stone Co. v. Dickason*, 276 Ill. 590, 115 N. E. 176, aff'g 199 Ill. App. 640.

⁴⁸ *Wicks Stone Co. v. Dickason*, 276 Ill. 590, 115 N. E. 176, aff'g 199 Ill. App. 640.

⁴⁹ Subscriptions to stock, when cause of action accrues for instalments, see *Grice v. Anderson*, 109 S. C. 388, 96 S. E. 222.

⁵⁰ *Bauman v. Kiskadden*, 94 Ohio St. 130, 113 N. E. 588.

⁵¹ *Grice v. Anderson*, — N. C. —, 96 S. E. 222.

⁵² See also § 4100, *infra*.

⁵³ *Philadelphia Motor Speedway Ass'n v. Sale*, 69 Pa. Super. Ct. 583.

⁵⁴ *Hauger v. International Trading Co.*, 184 Ky. 794, 214 S. W. 438.

⁵⁵ *United German Silver Co. v. Bronson*, 92 Conn. 266, 102 Atl. 647.

of stock surrendered.⁵⁶ Failure of the corporation to file or present a claim in probate court for liability of deceased on unpaid subscription bars a recovery by it of such unpaid balance.⁵⁷

By statute in some states all the stockholders may be sued by the corporation together in one suit for unpaid subscriptions.⁵⁸ In Pennsylvania, by statute, actions for unpaid subscriptions may be united and all brought in one county regardless of the stockholders being residents of different counties; but separate suits cannot be brought in one county and part of defendants served in other counties.⁵⁹ Independently of statutes the liability of subscribers for unpaid subscriptions is several and not joint.⁶⁰

Actions by the same corporation to recover from the same defendant a balance due on a stock subscription, where the issues were practically the same in all the cases, are properly consolidated.⁶¹

§ 658. — Effect of remedy by forfeiture or sale of shares.

For failure to pay instalments, the subscription contract is sometimes construed to warrant a forfeiture of instalments paid as the only remedy.⁶² In California, in case of delinquency in paying a call for a part or all of an unpaid subscription, the corporation may either sue to collect the money or sell the stock, and the action may be brought before the date fixed for the sale.⁶³

§ 660. — Evidence and burden of proof; variance.⁶⁴ Articles of incorporation are admissible to show, as against the corpora-

⁵⁶ *Murphy v. Panton*, 96 Wash. 637, 165 Pac. 1074.

⁵⁷ *Geary St., P. & O. R. Co. v. Bradbury Estate Co.*, 179 Cal. 46, 175 Pac. 457.

⁵⁸ *Pittsburgh Wholesale Grocery Co. v. Rearich*, 67 Pa. Super. Ct. 490.

⁵⁹ *Pittsburgh Wholesale Grocery Co. v. Rearich*, 67 Pa. Super. Ct. 490.

⁶⁰ *In re Phoenix Hardware Co.*, 249 Fed. 410.

⁶¹ *Columbia-Knickerbocker Trust*

Co. v. Abbot, 247 Fed. 833.

⁶² *Denman v. Country Club Realty Co.*, — Ark. —, 220 S. W. 824.

⁶³ *Imperial Land & Stock Co. v. Oster*, 34 Cal. App. 776, 168 Pac. 1159.

⁶⁴ Evidence admissible in actions to enforce subscriptions where the defense is that they were procured by fraud, see *Columbia-Knickerbocker Trust Co. v. Abbot*, 247 Fed. 833.

tion seeking to recover an unpaid subscription, that all its capital stock had been subscribed for prior to defendant's subscription.⁶⁵

§ 661. — **Set-off and counterclaim by subscriber.** A debt owing a subscriber may, by agreement, be credited on the amount of the subscription.⁶⁶ But a subscriber, having an unliquidated claim against the corporation for services, cannot go into equity and have the claim there liquidated and set off against the amount due on his subscription.⁶⁷

§ 662. **Forfeiture and sale of shares—The right and power in general.** A subscription contract giving the corporation, as a sole remedy for failure to pay for stock, the right to forfeit instalments paid, is valid where no rights of creditors are involved and there is no statute to the contrary.⁶⁸ A contract right to forfeit instalments paid on subscriptions, for failure to pay subsequent instalments, will be presumed to have been exercised, so as to prevent an action for the balance, where no action is brought for five years after default.⁶⁹

VII. CALLS OR ASSESSMENTS ON UNPAID SUBSCRIPTIONS

§ 669. **When calls are necessary—In general.**⁷⁰ Generally, liability on unpaid subscriptions does not accrue until a call is made by the board of directors.⁷¹ A cause of action in favor of a corporation for the balance on an unpaid subscription does not accrue, within the statute of limitations, until the levy of an assessment and the issuance of a call.⁷²

§ 674. **Validity and sufficiency of calls—Time of making calls.** The Nevada statute authorizing corporations formed

⁶⁵ *Morrill v. Harris*, 23 N. M. 146, 167 Pac. 276.

⁶⁶ *Brockway v. Ready Built House Co.*, 95 Ore. 386, 187 Pac. 1038.

⁶⁷ *Brockway v. Ready Built House Co.*, 95 Ore. 386, 187 Pac. 1038.

⁶⁸ *Denman v. Country Club Realty Co.*, — Ark. —, 220 S. W. 824.

⁶⁹ *Denman v. Country Club Realty Co.*, — Ark. —, 220 S. W. 824.

⁷⁰ See also § 4134, *infra*.

⁷¹ *Lake Jackson Hotel Co. v. Rodwell*, 202 Ala. 216, 80 So. 38.

⁷² *In re Phoenix Hardware Co.*, 249 Fed. 410; *Geary St., P. & O. R. Co. v. Bradbury Estate Co.*, 179 Cal. 46, 175 Pac. 457.

thereunder to commence business when one thousand dollars of the capital stock is subscribed, permits a levy of assessments on unpaid stock as soon as such an amount is subscribed.⁷³

§ 677. — Uniformity and equality. A call is not unequal because for such an amount against the stock of some of the stockholders as would make their payments equal to the payments already made by other stockholders.⁷⁴

§ 678. — Mode of making calls. In California, an action does not lie on an unpaid subscription until the procedure prescribed by section 331 of the Civil Code has been complied with.⁷⁵

§ 683. Notice of calls and demand of payment—Necessity for notice. Demand need not be made before suing to recover a call, where notice of the call is properly given.⁷⁶

IX. INTEREST, PENALTIES AND LIQUIDATED DAMAGES

§ 689. Interest. In Maryland, interest on a subscription is not recoverable as matter of right.⁷⁷ Interest on duebills given for the price of stock runs only from demand of payment.⁷⁸

X. SUBSCRIPTION OF FULL AMOUNT OF CAPITAL STOCK, OR OF A SPECIFIED PERCENTAGE THEREOF

§ 692. As a condition precedent to legal incorporation or transaction of business.⁷⁹

⁷³ *McCarty v. Moore*, — Cal. —, 186 Pac. 140.

⁷⁴ *Imperial Land & Stock Co. v. Oster*, 34 Cal. App. 776, 168 Pac. 1159.

⁷⁵ *Bell Development Co. v. Marshall*, 35 Cal. App. 324, 169 Pac. 717.

⁷⁶ *Imperial Land & Stock Co. v. Oster*, 34 Cal. App. 776, 168 Pac. 1159.

⁷⁷ *Bucher v. Federal Baseball Club of Baltimore*, 130 Md. 635, 101 Atl. 534.

⁷⁸ *Thompson v. Schoch*, 254 Pa. 585, 99 Atl. 72.

⁷⁹ Nevada statutes as to amount of subscriptions necessary to enable corporation to commence business, see *McCarty v. Moore*, — Cal. —, 186 Pac. 140.

Under the Ohio statutes, the mere filing of the articles of incorporation in due form does not create the corporation, but there must be the ten per cent subscription to stock and payment of ten per cent before the corporation is

§ 693. As a condition precedent to enforcement of subscriptions—General rule.⁸⁰ Where it is not provided by statute what portion of corporate stock must be subscribed for before the corporation may do business, the general rule that no recovery can be had on a stock subscription until all the stock is subscribed is applicable.⁸¹

§ 694. — Effect of provisions of statute, charter or contract. Under the New York statute prohibiting a corporation from incurring any debt until the capital specified in its certificate of incorporation as the amount with which it will begin business has been paid in in money or property, the company may transact business if such amount is paid in although the entire stock is not subscribed, and subscriptions are binding although all the stock is not subscribed.⁸² A statute requiring half of the stock to be subscribed for before a corporation can transact business with persons other than its stockholders is no defense to an action on a stock subscription made before half of the stock has been subscribed.⁸³

§ 696. What subscriptions or promises may be counted.⁸⁴ The burden of showing some of the subscriptions are fraudulent or worthless is on the party setting up such defense.⁸⁵

§ 704. Waiver and estoppel—General principles. Subscribers cannot defend on the ground that the corporation was organized

created. *Parkside Cemetery Ass'n v. Cleveland, B. & G. Lake Traction Co.*, 93 Ohio St. 161, Ann. Cas. 1918 C 1051, 112 N. E. 596.

Statutory liability of stockholders where business commenced before minimum capital stock subscribed, see § 4156, *infra*.

⁸⁰ Note on "Liability on stock subscription as dependent upon whole amount of stock having been subscribed," see Ann. Cas. 1918 B 1137.

⁸¹ *Enterprise Sheet Metal Works v. Schendel*, — Mont. —, 173 Pac. 1059, holding also that certain allegations in the complaint did not show full subscription.

⁸² *Whalen v. Hudson Hotel Co.*, 183 N. Y. App. Div. 316, 170 N. Y. Supp. 855.

⁸³ *Hauger v. International Trading Co.*, 184 Ky. 794, 214 S. W. 438.

⁸⁴ Whether oral subscriptions to stock are to be counted, in determining whether half of the stock had been subscribed, as required by statute, where stockholder sued by creditor for his debt under such a statute, see *Shadbolt & Boyd Iron Co. v. Long*, — Wis. —, 179 N. W. 785, where question referred to but not decided.

⁸⁵ *Bunn v. Farmers' Warehouse Co.*, 18 Ga. App. 567, 90 S. E. 78.

and transacted business before its minimum capital stock was subscribed, as against a trustee in bankruptcy, where credit was extended the corporation on the faith of the validity of the stock subscriptions.⁸⁶

§ 705. — Particular acts constituting waiver or estoppel.

The right of a stockholder to defend against a call for his unpaid subscription on the ground that all the capital stock was not subscribed for is waived by his acting as president and director for a year after his subscription and his receiving a substantial salary during all of which time he knew that but a small part of the capital was subscribed.⁸⁷

XI. PAYMENTS ON SUBSCRIPTIONS

§ 707. Effect of nonpayment on legality of incorporation or right to commence business. In New York a payment of ten per cent of the subscription is a condition precedent to its right to do business,⁸⁸ but such statute requiring subscribers to pay ten per cent of the amount of their subscriptions at the time of subscribing applies only to subscriptions after incorporation.⁸⁹

A fictitious payment cannot be counted to show a compliance with a statutory provision that no corporation shall incur debts until the capital specified in its certificate of incorporation as the amount with which it will begin business shall have been paid in in money or property.⁹⁰

§ 708. Effect of nonpayment on validity of subscriptions and liability of subscribers. In New York, payment of ten per cent of a subscription, after organization, is a condition precedent to its validity.⁹¹ In that state, an option given by a corporation to purchase stock, without any payment in cash—the statute

⁸⁶ Chappell v. Lowe, 145 Ga. 717, 89 S. E. 777.

⁸⁷ Rogers v. Baird, 167 N. Y. Supp. 35.

⁸⁸ Whalen v. Hudson Hotel Co., 183 N. Y. App. Div. 316, 170 N. Y. Supp. 855.

⁸⁹ Rogers v. Baird, 167 N. Y. Supp. 35.

⁹⁰ Whalen v. Hudson Hotel Co., 183 N. Y. App. Div. 316, 170 N. Y. Supp. 855.

⁹¹ Primos Chemical Co. v. Fulton Steel Corporation, 266 Fed. 937; Whalen v. Hudson Hotel Co., 183 N. Y. App. Div. 316, 170 N. Y. Supp. 855.

requiring payment of ten per cent to make subscriptions to stock valid—does not constitute a subscription and is void.⁹² One who paid on his stock a few dollars less than the ten per cent required by the New York statutes, and paid nothing more, is not a stockholder who can be held liable for unpaid subscription on insolvency of the company, there being no conduct making the repudiation inequitable and unjust.⁹³ But a subscription is not invalid in New York because a short interval of time occurs between the subscription and the payment of the ten per cent.⁹⁴ So it is no defense to an action to recover the balance on a stock subscription that ten per cent of the amount subscribed was not paid by defendant in cash as required by the statute, where he acted as director and accepted dividends on all his stock, paid down a small amount on his subscription, and sold the stock, on the ground of public policy.⁹⁵ Subscribers to stock are entitled to a cancellation of their subscription where procured by false representations of the promoters and before the amount was paid in as required by statute to authorize the corporation to commence business.⁹⁶ Subscribers entitled to cancel their subscriptions, because of fraud and because all the stock was not paid for as required, are not liable for debts incurred by the promoters.⁹⁷

In Texas, it seems, each subscriber need not pay in fifty per cent of his subscription before subscription contracts become binding, but it is sufficient that fifty per cent of the whole capital be paid in.⁹⁸ The provision in that state that half of each subscription must be paid before incorporation cannot be set up as a defense by a stockholder who actively assisted in incorporating the company with knowledge that such payments had not been made.⁹⁹

⁹² *Donovan v. Powers Film Products*, 111 N. Y. Misc. 276, 181 N. Y. Supp. 157.

⁹³ *Mills v. Friedman*, 111 N. Y. Misc. 253, 181 N. Y. Supp. 285.

⁹⁴ *Mills v. Friedman*, 111 N. Y. Misc. 253, 181 N. Y. Supp. 285.

⁹⁵ *Jeffery v. Selwyn*, 220 N. Y. 77, 6 A. L. R. 1111, 115 N. E. 275, aff'g 173 N. Y. App. Div. 217, 159 N. Y. Supp. 430.

⁹⁶ *Whalen v. Hudson Hotel Co.*,

183 N. Y. App. Div. 316, 170 N. Y. Supp. 855.

⁹⁷ *Whalen v. Hudson Hotel Co.*, 183 N. Y. App. Div. 316, 170 N. Y. Supp. 855.

⁹⁸ *Stringfellow v. Panhandle Packing Co.*, — Tex. —, 213 S. W. 250.

⁹⁹ *Stringfellow v. Panhandle Packing Co.*, — Tex. —, 213 S. W. 250.

The "effect upon the validity of the subscription to corporate stock, of failure to comply with statutory requirements of payment at the time of subscribing" is the subject of an extensive note in a recent volume of the American Law Reports.¹

§ 712. Sufficiency of payment.² Subscriptions are payable in cash unless otherwise provided.³ If payment for the stock is to be paid in land, the subscriber cannot be held liable in money except in case of his refusal or inability to convey the land.⁴ The fact that the capital of a company increases in value after its organization does not operate as a payment by the stockholders on their stock.⁵ Stock is not paid in full merely because the holder thereafter performs certain voluntary labor for the company so that the value of the assets exceeds the amount of the capital stock.⁶ If stock is sold under an agreement that the balance over and above the cash payment and a note given will be satisfied out of stock dividends, the purchaser need not demand an application of dividends to enable him to defend an action for the balance.⁷ The corporation is liable for money received by its agent for selling stock, from a sale of other stock put up as a part of the price to be paid for stock in the agent's corporation, where the agent was authorized to re-

¹ 6 Am. Law Rep. 1116-1134, annotating *Jeffery v. Selwyn*, 220 N. Y. 77, 6 A. L. R. 1111, 115 N. E. 275.

² See also § 570, *supra*.

Transaction construed as payment for subscription to stock in cash or securities, and that notes given by subscriber represented obligation on agreement to pay certain sum into surplus funds as consideration for permission to subscribe, see *Commonwealth Bonding & Casualty Ins. Co. v. Hollifield*, — Tex. —, 220 S. W. 322.

Construction of agreement to pay for stock in radiators, as to necessity for demand for the radiators within specified time, see

Lawrence v. Fedders, 166 N. Y. Supp. 335.

Transaction held an absolute exchange or payment for stock in real property, see *Fogarty v. Hunter*, 83 Ore. 183, 162 Pac. 964.

³ *Brockway v. Ready Built House Co.*, 95 Ore. 386, 187 Pac. 1038.

⁴ *Natwick v. Terwilliger*, 24 Wyo. 253, 160 Pac. 338.

⁵ *In re Caledonia Coal Co.*, 254 Fed. 742, 746.

⁶ *In re Caledonia Coal Co.*, 254 Fed. 742, 746.

⁷ *Mid-Continent Life Ins. Co. v. Beasley*, 202 Ala. 35, 79 So. 373, holding also that facts did not show waiver of such special agreement.

ceive such stock in payment.⁸ Payment by a third person is sufficient.⁹

Additional sums which a subscriber contracts to pay in excess of the legal value of the shares subscribed should not be considered as payments for such shares.¹⁰

XII. OVERSUBSCRIPTION AND APPORTIONMENT OR DISTRIBUTION OF STOCK

§ 713. Effect of oversubscription. It is a defense to a suit to enforce payment of a subscription to stock that the total authorized capital stock had been fully subscribed before defendant subscribed.¹¹

XIII. ESTOPPEL OF SUBSCRIBERS

§ 716. Estoppel to deny subscription or the validity thereof. A subscriber may be estopped, by his conduct, to deny the validity of his subscription.¹² Thus, a person cannot lend his good name to a promoter to assist him in getting other people to take stock and then escape liability on an agreement that he would not be required to pay.¹³ So a subscriber is estopped to deny liability as stockholder where he has taken no steps to repudiate his subscription but instead has attended corporate meetings, given proxies, etc.¹⁴ Representations to prospective purchasers of stock that the speaker had subscribed to the stock does not estop him, as against the corporation, from attacking the validity of the subscription.¹⁵

⁸ *Bissell v. M. W. Savage Factories*, 137 Minn. 131, 162 N. W. 1066.

⁹ *Central Trust Co. v. Crawford*, 201 Ill. App. 555.

¹⁰ *Commonwealth Bonding & Casualty Ins. Co. v. Hollifield*, — Tex. —, 220 S. W. 332.

¹¹ *Morrill v. Harris*, 23 N. M. 146, 167 Pac. 276.

¹² *Re Port Arthur Wagon Co.*, 45 Dom. L. Rep. (Can.) 207.

¹³ *Boushall v. Stronach*, 172 N. C. 273, 90 S. E. 198.

¹⁴ *Traders Trust Co. v. Goodman*, 37 Dom. L. Rep. (Can.) 31.

¹⁵ *Primos Chemical Co. v. Fulton Steel Corporation*, 266 Fed. 937.

CHAPTER 18

NAME

- § 722. Name which may be adopted—In general.
- § 723. — Effect of National Banking Act.
- § 724. Refusal of charter or license under identical or similar name.
- § 725. Injunction against use of identical or similar name in general.
- § 726. Unfair competition—In general.
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- § 736. — Injunction by foreign corporation against domestic corporation.
- § 738. Legal name—In general.
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- § 742. Effect of misnomer—In grants, conveyances, contracts, wills, etc.
- § 743. — In pleadings, process, etc.
- § 744. Change of name—Right in general.
- § 745. — Name which may be adopted.
- § 746. — Mode of changing name.
- § 747. — Effect of change.

§ 722. Name which may be adopted—In general. In New York the name "Antipoller Mutual Aid Society" can be applied only to a company incorporated under the Banking or the Insurance Law.¹ The same rule applies to the name "Howard Aid Society."² "The W. B. Manufacturing Company" was held entitled to enjoin the use of the name "R. B. Manufacturing Company," where misleading, although the latter is an abbreviation for "Rubenstein Brothers," since two or more detached and separated letters of the alphabet do not constitute a name.³

¹ In re Antipoller Mut. Aid Society, 100 N. Y. Misc. 589, 166 N. Y. Supp. 386. ard Aid Society, 160 N. Y. Supp. 789.

² In re Incorporation of Howard Aid Society, 128 N. E. 21.

§ 723. — Effect of National Banking Act. Where there is federal authority for the use of a certain name by a national bank, a state cannot compel a change in the name.⁴

§ 724. Refusal of charter or license under identical or similar name. The determination of the secretary of state in accepting articles of incorporation for filing that the corporate name is not so similar as to be misleading does not preclude the right of a court to enjoin the use of such name as so similar to that of another corporation as to be misleading.⁵ In Pennsylvania the superior court refused to review the discretion of the common pleas in refusing to grant a charter to the "Matki Boski Bolesne Polish National Catholic Church" where there was a church in the same town known as the Polish Catholic Church.⁶

§ 725. Injunction against use of identical or similar name in general.⁷ A corporation cannot sue to protect its commonly called or fictitious name but only its corporate name.⁸ Use of a corporate name cannot be enjoined merely because it resembles in part the name of another corporation.⁹ A new company having a name similar to an old company may be enjoined from applying for registration without waiting until the company actually commences to do business, where the name would deceive the public.¹⁰ Laches in suing ordinarily is not a defense

⁴ *Fidelity Nat. Bank & Trust Co. of Kansas City v. Enright*, 264 Fed. 236.

⁵ *Diamond Drill Contracting Co. v. International Drill Contracting Co.*, 106 Wash. 72, 179 Pac. 120.

⁶ *In re Incorporation of Matki Boski Bolesne Polish National Catholic Church*, 67 Pa. Super. Ct. 493.

⁷ "Daughters of, Isabella" of Connecticut was held not entitled to enjoin a national organization from using that name, especially where guilty of laches. *National Circle Daughters of Isabella v. National Order of Daughters of Isabella*, 252 Fed. 815. See also same case, 232 Fed. 907.

⁸ *Detroit Sav. Bank v. Highland Park State Bank of Detroit*, 201 Mich. 601, 167 N. W. 895. But see case cited in vol. 2, p. 1643, note 32.

A corporation cannot complain of the use by another corporation of a name by which the complaining corporation was known; where not its true corporate name. *Dubuque German College v. St. Joseph's College*, — Iowa —, 169 N. W. 405.

⁹ *John Palmer Co. v. Palmer-McLellan Shoe-Pack Co.*, 37 Dom. L. Rep. (Can.) 201.

¹⁰ *Guardian Assurance Co. v. Garrett*, 40 Dom. L. Rep. (Can.) 455.

in an injunction suit.¹¹ If names are so similar that the public would be deceived thereby to the injury of complainant, a temporary injunction may issue.¹²

§ 726. Unfair competition—In general.¹³ The better view is that actual fraud need not be alleged nor proved, and that constructive fraud is sufficient, and this is the rule in Alabama.¹⁴

The names "Svenska National Forbundet" and "Swedish National Association" are not similar except in meaning.¹⁵ The name "International Diamond Drill Contracting Company" was held not so similar to the same name with the word "International" left off as to be misleading.¹⁶ Use of name "Auto Sales and Parts Company" constituted unfair competition with name "Auto Parts Company."¹⁷ The names "Thompson Lumber Company" and "Thompson Yards, Incorporated" are not so alike that the mere use of the latter is a fraud or constitutes unfair competition.¹⁸ The "Chaffee Brothers Furniture Company" is not so similar a name to the "Young & Chaffee Furniture Company" as to show unfair competition.¹⁹ The words "United Painless Dentists" were held so similar to "Union Painless Dentists" as to constitute unfair competition.²⁰ The name "G. B. McVay & Son Seed Co." was held an unfair use as against the "McVay Seed & Floral Co." where calculated to deceive the public and appropriate more or less of the trade of the latter.²¹ The name "J. N. Lapointe Co." is not neces-

¹¹ *Oklahoma Producing & Refining Co. v. Oklahoma Consol. Producing & Refining Co.*, — Del. Ch. —, 106 Atl. 38.

¹² *Oklahoma Producing & Refining Co. v. Oklahoma Consol. Producing & Refining Co.*, — Del. Ch. —, 106 Atl. 38.

¹³ Note on "Use of personal or corporate trade name as unfair competition," see *Ann. Cas.* 1918 A 229.

¹⁴ *G. B. McVay & Son Seed Co. v. McVay Seed & Floral Co.*, 201 Ala. 644, 79 So. 116.

¹⁵ *Svenska National Förbundet i Chicago v. Swedish National Ass'n*, 205 Ill. App. 428.

¹⁶ *Diamond Drill Contracting Co. v. International Drill Contracting Co.*, 106 Wash. 72, 179 Pac. 120.

¹⁷ *Auto Parts Co. v. Silverstein*, 211 Ill. App. 436.

¹⁸ *Thompson Lumber Co. v. Thompson Yards, Inc.*, 144 Minn. 298, 175 N. W. 550.

¹⁹ *Young & Chaffee Furniture Co. v. Chaffee Bros. Furniture Co.*, 204 Mich. 293, 170 N. W. 48.

²⁰ *Aultz v. Zucht*, — Tex. Civ. App. —, 209 S. W. 475.

²¹ *G. B. McVay & Son Seed Co. v. McVay Seed & Floral Co.*, 201 Ala. 644, 79 So. 116.

sarily unfair competition as against the "Lapointe Machine Tool Co."²² A bank may use the word "Detroit" as part of its corporate name although such word is used in the names of other banks in the city.²³

One's own name may be used in a corporate name where not done to mislead nor in fact misleading.²⁴ While every person has a natural right to the use of his own name for the designation of his business, yet the use of such name may constitute unfair use, where fraudulent.²⁵ The right exists to use a man's own name, as a part of a corporate name, where not selected for the purpose of unfair competition, although it may injure the business of another with the same name.²⁶ A corporation cannot adopt a name of a stockholder as part of its name where

²² *Lapointe Machine Tool Co. v. J. N. Lapointe Co.*, 115 Me. 472, 99 Atl. 348.

²³ *Detroit Sav. Bank v. Highland Park State Bank of Detroit*, 201 Mich. 601, 167 N. W. 895.

"The Detroit Savings Bank" cannot enjoin the use by another bank of the name "Bank of Detroit." *Detroit Sav. Bank v. Highland Park State Bank of Detroit*, 201 Mich. 601, 167 N. W. 895.

²⁴ *W. R. Speare Co. v. Speare*, 265 Fed. 876; *Tharp-Bultman-Sontheimer Co. v. Tharp-Sontheimer-Tharp*, 147 La. 765, 85 So. 906; *Young & Chaffee Furniture Co. v. Chaffee Bros. Furniture Co.*, 204 Mich. 293, 170 N. W. 48.

Where no confusion exists, a man may use his own name as part of a corporate name although such name is already in use as a corporate name. *Henry Romeike v. Albert Romeike & Co.*, 179 N. Y. App. Div. 712, 167 N. Y. Supp. 235.

A person may use his full name as part of a corporate name although incidentally interfering with the competing business of another who has the same last name.

Burns v. William J. Burns International Detective Agency, — Mass. —, 127 N. E. 334.

A man may use his own name as part of a corporate name where it does not deceive purchasers into thinking the goods to be manufactured by a corporation organized at an earlier date. *Deister Concentrator Co. v. Deister Mach. Co.*, 63 Ind. App. 412, 112 N. E. 906, 114 N. E. 485.

²⁵ *G. B. McVay & Son Seed Co. v. McVay Seed & Floral Co.*, 201 Ala. 644, 79 So. 116.

Use of one's name as part of a corporate name, where calculated to deceive the public and in fraud of the rights of another corporation, may be enjoined. *G. B. McVay & Son Seed Co. v. McVay Seed & Floral Co.*, 201 Ala. 644, 79 So. 116.

Use of a person's name, where he is merely a nominal stockholder, may, it seems, show unfair use. *G. B. McVay & Son Seed Co. v. McVay Seed & Floral Co.*, 201 Ala. 644, 79 So. 116.

²⁶ *Gallet v. R. & G. Soap & Supply Co.*, 254 Fed. 802, applying rule to use of letters "R. & G." as initials of organizers.

its use will have the effect of deceiving or misleading the public.²⁷ Where a corporation had been enjoined from using the word "Rogers" in connection with silver-plated ware, and thereafter the stockholders formed a new corporation after taking in a skilled silver worker named H. O. Rogers merely to use his name, the manufacture of silver-plated ware by the new company under the name of "Rogers" is unfair competition.²⁸ If an individual sells his business and the use of his name to a corporation, he may be enjoined from thereafter using his name as part of a corporate name in the same business.²⁹ An inventor who has transferred his patent rights to a corporation bearing his family name may use his own name in a new corporation, on withdrawing from the old.³⁰

An interesting case arose in Minnesota where the Review Publishing Company of St. Paul, doing a job printing business, consented to the use of their name in Minneapolis by a partnership formed by its managing officer and others. Thereafter the partnership having adopted the name in its Minneapolis business, was incorporated under a different name. The St. Paul company, afterwards, established a branch in Minneapolis and attempted to divert the business built up originally by the partnership. The new company sued to enjoin the St. Paul company from using its name in Minneapolis without any distinguishing words. The court enjoined further interference by the St. Paul corporation with the right of plaintiff to use its name in its business in Minneapolis and required it, if it desired to continue business in Minneapolis, to advertise its presence as "of St. Paul."³¹

A man may use his own name as a part of a corporate name provided it is not so similar to that of an existing corporation that the necessary result is loss to the latter, or the selection of the name is with a view to deceive. *Thompson Lumber Co. v. Thompson Yards, Inc.*, 144 Minn. 298, 175 N. W. 550.

²⁷ *M. M. Newcomer Co. v. Newcomer's New Store*, 142 Tenn. 108, 217 S. W. 822, where use of name "Newcomer's New Store" was

enjoined by the "M. M. Newcomer Company."

²⁸ *Wm. A. Rogers, Ltd. v. H. O. Rogers Silver Co.*, 237 Fed. 887.

²⁹ *Wheeler Syndicate v. Wheeler*, 99 N. Y. Misc. 289, 163 N. Y. Supp. 817.

³⁰ *Lapointe Machine Tool Co. v. J. N. Lapointe Co.*, 115 Me. 472, 99 Atl. 348.

³¹ *Twin City Brief Printing Co. v. Review Pub. Co.*, 139 Minn. 358, L. R. A. 1918 D 154, 166 N. W. 413.

§ 728. — Character of corporations entitled to protect names. Injunctive relief can be obtained by a religious corporation.³² But there is no sufficient similarity in the names “Polish National Catholic Church of the Holy Mother of the Rosary” and “Queen of the Most Holy Rosary” as to warrant injunctive relief.³³

§ 729. — When injunction will lie in general. The remedy for unfair competition is merely an injunction against doing competing business under plaintiff’s trade-mark name without enjoining the continued use of such name as a corporate name where it has other noncompeting business.³⁴

§ 730. — Basis of injunction. The name must actually deceive the public, it is held in some cases.³⁵

§ 731. — Generic terms.³⁶ There is no exclusive right to the use of the words “Material Men’s” as part of a corporate name.³⁷ The words “Diamond Drill Contracting Company” are not such that an exclusive right to their use can be acquired.³⁸ The word “Rosary,” used by the general public for a long period of time prior to its use in a corporate name, is public property and its use cannot be enjoined.³⁹ The phrase “Title Guarantee Company” is not such a one that a corporation can have a proprietary interest in such descriptive words.⁴⁰

In some of the states, including South Dakota and California,

³² *In re Baker*, 94 N. Y. Misc. 661, 158 N. Y. Supp. 632; *Polish National Catholic Church of Holy Mother of Rosary v. Diocese of Buffalo*, 171 N. Y. Supp. 401.

³³ *Polish National Catholic Church of Holy Mother of Rosary v. Diocese of Buffalo*, 171 N. Y. Supp. 401. See also *In re Baker*, 94 N. Y. Misc. 661, 158 N. Y. Supp. 632.

³⁴ *Parsons Trading Co. v. Hoffman*, 107 N. Y. Misc. 536, 177 N. Y. Supp. 713.

³⁵ *Polish National Catholic Church of Holy Mother of Rosary v. Diocese of Buffalo*, 171 N. Y. Supp. 401.

³⁶ See also § 722, *supra*.

³⁷ *Material Men’s Mercantile Ass’n v. Material Men’s Credit Agency*, 191 N. Y. App. Div. 73, 180 N. Y. Supp. 801.

³⁸ *Diamond Drill Contracting Co. v. International Drill Contracting Co.*, 106 Wash. 72, 179 Pac. 120.

³⁹ *Polish National Catholic Church of Holy Mother of Rosary v. Diocese of Buffalo*, 171 N. Y. Supp. 401.

⁴⁰ *Title & Mortgage Guarantee Co. v. Louisiana Abstract & Title Guarantee Co.*, 143 La. 894, 79 So. 529.

by statute, no exclusive right can be obtained to a corporate name relating merely to the place of business and the kind of business, such as "Jones County Abstract Company."⁴¹

§ 732. — Competition, deception and damage. Mere trivial facts such as confusion in delivery of mail or in transactions with telegraph and express companies are not sufficient.⁴² It is not necessary to show, in a bill for injunctive relief only, that any persons have been actually deceived.⁴³

An incorporated college cannot complain that the name of another college unfairly competes with the name of one of its departments.⁴⁴ For instance, it was held that the "Dubuque German College and Seminary" could not enjoin the "Dubuque College" from use of its name, as unfair competition, although a department of the complainant school is named "Dubuque College," where there is no competition between the schools and the only confusion was at times in the delivery of mail and goods.⁴⁵

§ 735. — Injunction by domestic corporation against foreign corporation. A domestic corporation which has taken the name of a foreign corporation, where the latter had not complied with the local laws as to doing business in the state, cannot enjoin the use of the name by the latter, but instead will be itself enjoined from using such name.⁴⁶

§ 736. — Injunction by foreign corporation against domestic corporation.⁴⁷ A corporation cannot appropriate the name of a foreign corporation and pirate its business merely because the foreign corporation has not complied with the laws of the state,

⁴¹ *Bidwell v. Collins*, 39 S. D. 395, 164 N. W. 969, following *Dunston v. Los Angeles Van & Storage Co.*, 165 Cal. 89, 131 Pac. 115.

⁴² *Polish National Catholic Church of Holy Mother of Rosary v. Diocese of Buffalo*, 171 N. Y. Supp. 401.

⁴³ *G. B. McVay & Son Seed Co. v. McVay Seed & Floral Co.*, 201 Ala. 644, 79 So. 116.

⁴⁴ *Dubuque German College v.*

St. Joseph's College, — Iowa —, 169 N. W. 405.

⁴⁵ *Dubuque German College v. St. Joseph's College*, — Iowa —, 169 N. W. 405.

⁴⁶ *General Film Co. of Missouri v. General Film Co. of Maine*, 237 Fed. 64.

⁴⁷ See generally on this subject, *General Film Co. of Missouri v. General Film Co. of Maine*, 237 Fed. 64.

although the secretary of state has approved the name by issuing the certificate of incorporation.⁴⁸

§ 738. Legal name—In general. A corporation has no right, in addition to the actual name given to it by its articles of incorporation, to a translation of such name into a foreign language.⁴⁹ A corporation which purchases the assets of another corporation acquires the right to the use of the corporate name, including the name of one of the officers.⁵⁰

§ 740. — Use of assumed name. In addition to the name given it by its charter, a corporation may acquire other names by user or reputation.⁵¹ If a corporation uses a name other than its corporate name, it can acquire no legal title to such additional name, however extensive such use may be.⁵² While a corporation may do business under an assumed or false name and be sued by such name, yet proof of incorporation by some name must be established.⁵³

§ 741. Statutory requirement of use of "Incorporated" in connection with name. A Kentucky statute requires corporations to paint or print their corporate name with the word "Incorporated" "on their principal place or places of business." ⁵⁴

§ 742. Effect of misnomer—In grants, conveyances, contracts, wills, etc.⁵⁵ Misnomer in signing a corporate contract is not fatal where there can be no mistake as to the corporation intended to be bound.⁵⁶ A contract made in a name other

⁴⁸ General Film Co. of Missouri v. General Film Co. of Maine, 237 Fed. 64.

⁴⁹ Svenska National Förbundet i Chicago v. Swedish National Ass'n, 205 Ill. App. 428.

⁵⁰ G. B. McVay & Son Seed Co. v. McVay Seed & Floral Co., 201 Ala. 644, 79 So. 116.

⁵¹ W. B. Clarkson & Co. v. Gans S. S. Line, — Tex. Civ. App. —, 187 S. W. 1106.

⁵² Svenska National Förbundet i Chicago v. Swedish National Ass'n, 205 Ill. App. 428.

⁵³ Simpson v. Grand Interna-

tional Brotherhood of Locomotive Engineers, 83 W. Va. 355, 98 S. E. 580.

⁵⁴ Western Oil Refining Co. v. Com., 180 Ky. 248, 202 S. W. 636, determining whether place in county where foreign oil company maintained stationary tanks was a "principal place of business."

⁵⁵ Mode of pleading misnomer, see § 3072, *infra*.

Amendment of pleading to correct, see § 3080, *infra*.

⁵⁶ Pilsen Brewing Co. v. Wallace, 214 Ill. App. 540.

than the true name of the corporation may be enforced by it where it has recognized the contract as its own and partly performed it.⁵⁷

Misnomer in a corporate deed is not fatal.⁵⁸ The inclusion or the exclusion of the word "the," where it is, or is not, properly a part of a corporate name, will not vitiate a grant of lands either to or by the corporation.⁵⁹

Misnomer does not defeat a legacy to a corporation where the intention is clear.⁶⁰

§ 743. — In pleadings, process, etc.⁶¹ Misnomer of defendant corporation in pleading is not fatal where it has been properly served with process, since the misnomer is subject to amendment in such a case.⁶² In one case it was held within the discretion of the trial court, on motion made by plaintiff several years after a default judgment, to correct the pleadings, process and judgment by substituting the word "Compressing" for the word "Gas" in the corporate name of defendant, where defendant had been sued under its generally known name.⁶³ A default judgment against a corporation will not be set aside because of a shortening of the corporate name in the summons, where the name was properly stated in the complaint and in the sheriff's return.⁶⁴

Variance in the corporate name in a criminal prosecution is ordinarily immaterial.⁶⁵

§ 744. Change of name—Right in general. A corporation cannot change its name unless authorized by law,⁶⁶ but courts will not interfere with a change of corporate name, at the in-

⁵⁷ *W. B. Clarkson & Co. v. Gans S. S. Line*, — Tex. Civ. App. —, 187 S. W. 1106.

⁵⁸ *Chew v. First Presbyterian Church of Wilmington, Delaware*, 237 Fed. 219.

⁵⁹ *Elbert v. Wilmington Turngemeinde*, — Del. —, 107 Atl. 215.

⁶⁰ *Kernoohan v. Farmers' Loan & Trust Co.*, 187 N. Y. App. Div. 668, 175 N. Y. Supp. 831.

⁶¹ See also § 747, *infra*.

⁶² *Thompson v. Southern Pac. Co.*, — Cal. —, 183 Pac. 153.

⁶³ *Gordon v. Pintsch Gas Co.*, 178 N. C. 435, 100 S. E. 878 (but see dissenting opinion of Justice Walker).

⁶⁴ *Tennessee River Nav. Co. v. Hodges*, 202 Ala. 15, 79 So. 300.

⁶⁵ *State v. Long*, 278 Mo. 379, 213 S. W. 436.

⁶⁶ *American Elementary Elec. Co. v. Normandy*, 46 App. Cas. (D. C.) 329, 339.

stance of minority stockholders, since relating to internal management.⁶⁷

A statute permitting any "person" to change his name is not applicable to corporations where the wording of the statute clearly indicates that it was intended to apply only to individuals.⁶⁸

An agreement to consolidate does not deprive the new corporation of the right to change its name.⁶⁹

§ 745. — Name which may be adopted. A change of name of a bank should not be allowed where injury to another bank is likely to be caused by confusion between its name and the new name.⁷⁰ In New York, a membership corporation may change its name from "Nyack Country Club" to "The Nyack Club."⁷¹

§ 746. — Mode of changing name. A corporation cannot change its name except as provided for by statute.⁷² An application for change of name should state all the material facts; and if the fact that the applicant was enjoined from using its original corporate name is concealed the order granting the application will be vacated.⁷³

A change of name approved by the stockholders and the secretary of state cannot be annulled by a court of equity, in Pennsylvania, where the secretary of state is vested with discretion to approve or disapprove changes of corporate names.⁷⁴

§ 747. — Effect of change. Legal identity is not affected by change of name⁷⁵ which does not have the effect of making a

⁶⁷ *In re Hinds, Noble & Eldredge*, 172 N. Y. App. Div. 140, 158 N. Y. Supp. 249.

⁶⁸ *American Elementary Elec. Co. v. Normandy*, 46 App. Cas. (D. C.) 329, 340.

⁶⁹ *In re Hinds, Noble & Eldredge*, 172 N. Y. App. Div. 140, 158 N. Y. Supp. 249.

⁷⁰ *In re Bank of Europe*, 109 N. Y. Misc. 363, 179 N. Y. Supp. 664.

⁷¹ *In re Nyack Country Club*, 166 N. Y. Supp. 611, distinguishing *In re American Cigar Lighter Co.*, 77 N. Y. Misc. 643, 138 N. Y. Supp. 455.

⁷² *Pilsen Brewing Co. v. Wallace*, 291 Ill. 59, 8 A. L. R. 579, 125 N. E. 714.

⁷³ *In re Baumann Furniture Co.*, 163 N. Y. Supp. 360.

⁷⁴ *People's Trust Co. of Pittsburgh v. Woods*, 263 Pa. 357, 106 Atl. 544, following *People's Trust Co. of Pittsburgh v. Safe Deposit & Trust Co. of Pittsburgh*, 259 Pa. 62, 102 Atl. 412.

⁷⁵ *Board of Com'rs Mattamuskeet Drain. Dist. v. A. V. Wills & Sons*, 236 Fed. 362; *Stewart v. Preston*, — Fla. —, 86 So. 348; *Terminal Ice & Power Co. v.*

new corporation.⁷⁶ A change of name, ineffectual for failure to comply with the statute, does not affect the liability of the corporation on its contracts.⁷⁷ A change of name of a corporation does not affect the validity of a notice of a mechanic's lien given in the old name as owner of the property.⁷⁸

A corporation which has changed its name may sue in the new name on any contract it could have recovered on under the old name, including a contract of guaranty running to the corporation under its old name.⁷⁹ If there has been a change of name, a contract made before the change may be sued on by the new name and it is sufficient to allege that the plaintiff entered into the contract by its former corporate name.⁸⁰ Where, after a corporation changed its name, a fidelity bond was executed to it in its old name and accepted by its agent, it could sue in its new name, on a breach of the bond, where the identity of the new corporation as the same as the old one is undisputed.⁸¹

Where the name of a corporation has been legally changed, it is suable in the new corporate name although the alleged cause of action may have arisen before the change.⁸² Where a corporation is sued by its old name, it may appear by its new name so as to preclude a decree pro confesso against the corporation in its old name.⁸³

American Fire Ins. Co. (Mo. App.), 187 S. W. 564.

An authorized change of corporate name has no more effect on corporate identity than a change in the name of a natural person has upon his identity. *C. R. Miller & Bro. v. Mummert*, — Tex. Civ. App. —, 196 S. W. 270.

⁷⁶ *W. T. Rawleigh Co. v. Grigg*, — Mo. App. —, 191 S. W. 1019, disapproving *Crane Co. v. Specht*, 39 Neb. 123, 42 Am. St. Rep. 562, 57 N. W. 1015; *W. T. Raleigh Medical Co. v. Bunning*, — Neb. —, 176 N. W. 85.

⁷⁷ *Pilsen Brewing Co. v. Wallace*, 291 Ill. 59, 8 A. L. R. 579, 125 N. E. 714.

⁷⁸ *Church E. Gates & Co. v. Na-*

tional Fair & Exposition Ass'n, 225 N. Y. 142, 121 N. E. 741.

⁷⁹ *T. W. Raleigh Medical Co. v. Bunning*, — Neb. —, 176 N. W. 85, expressly overruling *Crane Co. v. Specht*, 39 Neb. 123, 42 Am. St. Rep. 562, 57 N. W. 1015.

⁸⁰ *W. T. Rawleigh Co. v. Grigg*, — Mo. App. —, 191 S. W. 1019.

⁸¹ *Detroit Automatic Scale Co. v. Taylor*, — Okla. —, 169 Pac. 908, following *Peever Mercantile Co. v. State Mut. Fire Ins. Ass'n*, 23 S. D. 1, 19 Ann. Cas. 1236, 119 N. W. 1008.

⁸² *Porter v. State Grand Lodge No. 7*, 146 Ga. 13, 90 S. E. 281.

⁸³ *Stewart v. Preston*, — Fla. —, 86 So. 348.

CHAPTER 19

SEAL

§ 751. In general.

§ 752. Under charter or statute.

§ 753. Adoption and form.

§ 754. Simple contracts.

§ 756. Deeds and mortgages.

§ 757. Power to affix.

§ 759. Effect.

§ 751. In general. Unless the charter or governing statute requires it, a corporate act need not be evidenced by a seal except where a seal would be required of individuals.¹ The modern rule is that a seal is not necessary,² and want of a corporate seal on a contract is immaterial in case the contract is executed.³ However, it is held that specifications of objection to a bankrupt's discharge, where filed by a corporation, must be under the corporate seal.⁴

§ 752. Under charter or statute. Statutes generally require a seal in case of conveyances affecting real estate.⁵

Affixing the corporate seal several months after the execution of a contract, where not authorized by the corporation, does not cure the defect of the want of seal.⁶

§ 753. Adoption and form. Where the execution clause of a lease stated that "the said lessor has caused these presents to

¹Grand Lodge, Knights of Pythias v. State Bank, — Fla. —, 84 So. 528; State ex rel. Swearingen v. Watters, 75 Fla. 584, 78 So. 671.

²Commercial Security Co. v. Modesto Drug Co., — Cal. App. —, 184 Pac. 964.

³Foster v. British Colonial Fire Ins. Co., 37 Dom. L. Rep. (Can.) 404.

⁴In re Abramovitz, 253 Fed. 299.

⁵Bentley v. Zelma Oil Co., 76 Okla. 116, 184 Pac. 131, holding that conveyance of an interest in an oil and gas lease was a conveyance affecting real estate.

⁶West Penn Chemical & Manufacturing Co. v. Prentice, 236 Fed. 891.

be executed by J. H. McLaurin, its president," it is clearly an adoption of the seal used by the president in the execution of the instrument. The seal need not be the common seal of the corporation.⁷ A deed signed with the corporate name per a certain officer, with the word "seal" in brackets after the signature, where it contains the recital "Witness its hand and seal," is properly sealed so as to show the authority of the officer to sign the deed.⁸

§ 754. Simple contracts. The modern rule is that a corporation may be bound although the contract is not under seal.⁹ A corporate contract need not be under seal unless a similar contract made by an individual would require a seal.¹⁰ A conditional bill of sale by a corporation need not be under seal.¹¹

The rule that whenever the act of agency is required to be done in the name of the principal under seal, the authority to do the act must be conferred by an instrument under seal, does not apply to the appointment of an agent by a corporation.¹² Ratification of an agent's act in signing a bond need not be by a writing under seal.¹³

§ 756. Deeds and mortgages. In many states, a corporate mortgage need not be under seal.¹⁴ Deeds of corporations are

⁷ *Campbell v. McLaurin Inv. Co.*, 74 Fla. 501, 77 So. 277, distinguishing *Mitchell v. St. Andrews Bay Land Co.*, 4 Fla. 200.

⁸ *Boone v. Jenkins*, 147 Ga. 812, 95 S. E. 707, explaining decision in *Jenkins v. Boone*, 144 Ga. 44, 85 S. E. 1042.

⁹ *Commercial Security Co. v. Modesto Drug Co.*, — Cal. App. —, 184 Pac. 964, holding that absence of seal does not "justify even a suspicion that it was not executed by authority of the corporation."

An insurance company is bound by a contract to pay an agent for services although not under seal. *Foster v. British Colonial Fire Ins. Co.*, 37 Dom. L. Rep. (Can.) 404.

¹⁰ *Alabama Fidelity & Casualty Co. v. Jefferson County Sav. Bank*, 198 Ala. 557, 73 So. 918, and see § 751, *supra*.

¹¹ *Turner & Seymour Mfg. Co. v. Acme Mfg. Co.*, — N. J. Eq. —, 110 Atl. 123.

¹² *Alabama Fidelity & Casualty Co. v. Jefferson County Sav. Bank*, 198 Ala. 557, 73 So. 918.

¹³ *Alabama Fidelity & Casualty Co. v. Jefferson County Sav. Bank*, 198 Ala. 557, 73 So. 918.

¹⁴ *Millsaps v. Johnson*, — Tex. Civ. App. —, 196 S. W. 202.

A seal is not necessary to the validity of a chattel mortgage executed by a corporation. *P. R. Sinclair Coal Co. v. Missouri-Hydraulic Min. Co.*, — Mo. App. —, 207 S. W. 266.

often required by statute to be under seal.¹⁵ In Missouri, legal title does not pass under a deed of a corporation to which no seal is attached but the deed is good in equity.¹⁶ In Mississippi, an assignment of a deed of trust by a corporation need not be under seal nor need the assignment of a debt secured by a deed of trust, since not a corporate conveyance of real estate.¹⁷

§ 757. Power to affix.¹⁸ The seal is prima facie proof that it was attached by the proper authority.¹⁹

§ 759. Effect. Using the corporate seal makes the contract a specialty.²⁰ It is also prima facie evidence that the officers signing did not exceed their authority.²¹

¹⁵ Bentley v. Zelma Oil Co., 76 Okla. 116, 184 Pac. 131.

¹⁶ Albers v. Acme Paving & Crusher Co., 196 Mo. App. 265, 194 S. W. 61.

¹⁷ West v. Union Naval Stores Co., 116 Miss. 743, 77 So. 609.

¹⁸ See also § 1944, *infra*.

¹⁹ Macknight v. Davitt, 37 Cal.

App. 720, 174 Pac. 77; Heald v. Marden, Orth & Hastings Co., — N. Y. Misc. —, 172 N. Y. Supp. 25.

²⁰ Grand Lodge, Knights of Pythias v. State Bank, — Fla. —, 84 So. 528.

²¹ See § 1944, *infra*.

CHAPTER 20

CONSTRUCTION AND INTERPRETATION OF CHARTER

§ 770. General rules as to construction.

§ 771. Intention of legislature.

§ 772. Construction as a whole.

§ 773. Strict construction as to powers of company.

§ 770. General rules as to construction. The rule of contemporaneous construction applies to the interpretation of charters.¹

§ 771. Intention of legislature. A charter is to be construed so as to cover what is within its spirit as well as what is within its terms.²

§ 772. Construction as a whole. A charter is to be construed in all its parts as an entirety.³

§ 773. Strict construction as to powers of company.⁴ Whether corporate powers must be strictly construed depends upon who are the parties to a suit and the purpose for which it is brought.⁵

¹ Board of Chosen Freeholders v. Board of Public Utility Com'rs, 91 N. J. L. 97, 102 Atl. 1. v. Armstrong, 92 Conn. 349, 102 Atl. 791.

⁴ See also § 784, *infra*.

² Proprietors of Cornish Bridge v. Fitts, — N. H. —, 107 Atl. 626. ⁵ Cuero Packing Co. v. Alamo Mfg. Co., — Tex. Civ. App. —, 194

³ New York, N. H. & H. R. Co. S. W. 492.

CHAPTER 21

POWERS IN GENERAL

I. GENERAL RULES

- § 783. Inherent powers.
- § 784. Powers expressly conferred—In general.
- § 787. — As dependent on what statute incorporated under
- § 791. Powers implied from powers expressly granted.
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- § 840. Organization of subsidiary companies.
- § 841. Partnership—General rules.
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- § 857. Agricultural societies.
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- § 883. — Location of road.
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- § 895. Trust companies.
- § 898. Water companies.

I. GENERAL RULES

§ 783. Inherent powers. The only corporate powers are those conferred by the legislature either by express terms or by necessary implication.¹ A corporation has no inherent powers.²

§ 784. Powers expressly conferred—In general.³ The charter of a corporation, read in connection with the general laws applicable to it, is the measure of its powers;⁴ and such powers are to be determined by the law of the state in which it was created.⁵

Constitutions of some states prohibit “granting to any cor-

¹ *North American Union v. Johnson*, — Ark. —, 219 S. W. 769.

² *Citizens' Elec. Illuminating Co. v. Lackawanna & W. V. Power Co.*, 255 Pa. 176, 99 Atl. 465.

³ See also § 4348, *infra*.

For discussion of powers of corporations in Missouri, see *Orpheum Theater & Realty Co. v. Seavey & F. Brokerage Co.*, 197 Mo. App. 661, 199 S. W. 257.

⁴ *Alabama City, G. & A. R. Co. v. Kyle*, 202 Ala. 552, 81 So. 54.

A packing company, under the terms of its charter, was held to have power to maintain a refrigerating plant not theretofore erected by it. *Cuero Packing Co. v. Alamo Mfg. Co.*, — Tex. Civ. App. —, 194 S. W. 492.

⁵ *Hight v. Richmoud Park Imp. Co.*, 47 App. Cas. (D. C.) 518, 531.

poration * * * any special or exclusive privilege or immunity.' '6

§ 787. — As dependent on what statute incorporated under.⁷

§ 791. Powers implied from powers expressly granted.⁸

§ 793. **Extent of implied powers—In general.** A corporation has implied authority to do whatever is reasonably necessary to carry out the purposes of its existence;⁹ but a corporation without power to do a thing directly cannot accomplish the same purpose by indirection.¹⁰ It has well been said that "the authority of a corporation to perform a particular act is always dependent to a very considerable extent on the facts and circumstances existing at the time when it is proposed to perform the act."¹¹ In determining whether a given act is within the implied powers, the judgment of the directors and stockholders, while not conclusive, is entitled to consideration.¹²

The power of a corporation to do an act is not affected by the motive for the act.¹³

§ 794. — **Reasonably as distinguished from indispensably necessary.** The act need not be necessary in the sense of indispensable, to be within the implied powers of a corporation.¹⁴

⁶ Germantown Trust Co. v. Powell, — Pa. —, 108 Atl. 441.

⁷ Powers of corporations created by act of Congress, see article in 32 Harvard L. Rev. 689-708.

⁸ Definition of implied or incident powers, see Planters' Cotton Oil Co. v. Guaranty State Bank, — Tex. Civ. App. —, 188 S. W. 38.

For discussion of implied or incidental powers of corporations in general, see Texas Fidelity & Bonding Co. v. General Bonding & Casualty Ins. Co., — Tex. —, 216 S. W. 144.

⁹ Taylor Cotton Oil Co. v. Early-Foster Co., — Tex. Civ. App. —, 204 S. W. 1179.

Power to hold land includes power to preserve and improve it. Wilson v. Clinton Chapel African

Methodist Episcopal Zion Church, 138 Tenn. 398, 198 S. W. 244.

¹⁰ Messenheimer v. Fraternal Aid Union, 103 Kan. 552, 175 Pac. 679.

¹¹ Gause v. Commonwealth Trust Co., 196 N. Y. 134, 145, 24 L. R. A. (N. S.) 967, 89 N. E. 476, quoted as "the common sense rule" in New York Mail & Newspaper Transp. Co. v. Anderson, 234 Fed. 590, 593.

¹² Heinz v. National Bank of Commerce, 237 Fed. 942, 950.

¹³ Shera v. Merchants' Life Ins. Co., 237 Fed. 484, holding that "ultra vires is not affected by motives."

¹⁴ Heinz v. National Bank of Commerce, 237 Fed. 942.

§ 799. — **As affected by usage and custom.** A corporation can gain no implied franchise by usurping powers which the law forbids it to exercise, no matter how long continued.¹⁵

§ 804. **Mode of exercising powers.** A corporation organized for maintaining, operating and managing a system of safety vaults may carry on such business through the instrumentality of a lessee.¹⁶

§ 806. **Place of exercising powers—General rules.**¹⁷ Where the charter indicates where an electric light and power company may be located, the company can exercise its franchise only in the municipal or quasi municipal division in which it is located.¹⁸

§ 808. — **Power to act in other states.**¹⁹ A corporation has no power to perform strictly corporate acts outside the state of its creation;²⁰ but corporations may make contracts and carry on business outside the country in which they are incorporated where within powers in the home country and allowed by the laws of the foreign country.²¹ The power to act outside the state, as for instance in electing trustees, depends in some states on the nature of the corporation, i. e., whether one for pecuniary profit.²² A telegraph company incorporated in a state has no power to operate outside of the territory designated in its charter nor to accept business for places where it has no franchise.²³

¹⁵ Public Service Commission, Second Dist. v. J. & J. Rogers Co., 184 N. Y. App. Div. 705, 172 N. Y. Supp. 498.

¹⁶ La Salle v. Hamilton Nat. Bank, 204 Ill. App. 518.

¹⁷ See also § 869, *infra*.

¹⁸ Citizens' Elec. Illuminating Co. v. Lackawanna & W. V. Power Co., 255 Pa. 145, 99 Atl. 462.

¹⁹ Construction of charter of cement company as to power to acquire and operate property outside state, see Southwestern Portland Cement Co. v. Latta, — Tex. Civ. App. —, 193 S. W. 1115.

²⁰ Joseph T. Ryerson & Son v. Shaw, 277 Ill. 524, 115 N. E. 650.

²¹ Kittles v. Colonial Assurance Co., 35 Dom. L. Rep. (Can.) 588; Montreal-Canada Fire Ins. Co. v. National Trust Co., 35 Dom. L. Rep. (Can.) 445.

²² People v. Grant, 283 Ill. 391, 119 N. E. 344, *aff'd* 208 Ill. App. 235.

²³ People ex rel. Western U. Tel. Co. v. Public Service Commission of New York, Second Dist., — N. Y. App. Div. —, 183 N. Y. Supp. 659.

§ 810. Notice of extent of corporate powers. Notice of the extent of corporate powers is presumed as against persons dealing with a corporation.²⁴ But persons dealing with a corporation, while chargeable with knowledge of its powers, are not bound to take notice of the manner in which it has attempted to exercise the powers, "because its powers rest in the law, while the manner of the exercise of its powers rests in the facts."²⁵

§ 811. Evidence, presumptions and burden of proof. Acts of corporations "are presumed, in the absence of evidence to the contrary, to be within either the express or implied powers of the corporation."²⁶ There is a presumption that a corporation having power under some circumstances to do an act had power in a particular instance.²⁷ Power to do an accomplished act is presumed.²⁸ The burden of showing that contracts of a corporation are ultra vires rests on the party making such contention.²⁹

II. PARTICULAR ACTS

§ 818. Banking business. A corporation organized under the General Incorporation Act cannot engage in the business of banking or lending money.³⁰

§ 819. Business, trade or profession requiring license—Business or trade. Requiring a license of architects does not pre-

²⁴ *Orpheum Theater & Realty Co. v. Seavey & F. Brokerage Co.*, 197 Mo. App. 661, 199 S. W. 257; *Planters' Cotton Oil Co. v. Guaranty State Bank*, — Tex. Civ. App. —, 188 S. W. 38; *Tracy Loan & Trust Co. v. Merchants Bank*, 50 Utah 196, 167 Pac. 353, especially as to statutes defining the powers.

²⁵ *Thompson v. First State Bank*, — Tex. Civ. App. —, 211 S. W. 977.

²⁶ *Heinz v. National Bank of Commerce*, 237 Fed. 942, 952.

A corporation is presumed to

have acted within its powers. *Denecke v. West*, 184 Iowa 600, 169 N. W. 97.

²⁷ *Eckhart v. Heier*, 38 S. D. 524, 162 N. W. 150, where bank could under some circumstances enter into a contract of guaranty.

²⁸ *U. S. Industrial Alcohol Co. v. Distilling Co.*, — N. J. L. —, 104 Atl. 216.

²⁹ *Alabama City, G. & A. R. Co. v. Kyle*, 202 Ala. 552, 81 So. 54.

³⁰ *American Credit & Trust Co. v. New Era Chandelier Co.*, 208 Ill. App. 181.

clude a corporation doing an architectural business through licensed architects.³¹ A statute making it a misdemeanor to practice architecture without a certificate applies to persons only and not to corporations which may do an architectural business and sell plans prepared by certified architects.³² Making contracts for services to be performed by an architect and collecting the compensation therefor is not "practicing architecture," within the Illinois statute providing that no stock corporation shall be licensed to practice architecture.³³

§ 820. — **Practice of law.**³⁴ In New York, in construing the statute forbidding the formation of corporations to practice law, it is held that a corporation formed to furnish services to reduce assessments is engaged in the practice of law in violation of the statute;³⁵ that rendition of services in procuring reduction of assessment for taxation, where the corporation was not authorized to and did not bring certiorari, does not constitute the "practice of law";³⁶ that drawing a contract of sale, deed and mortgage as part of the examination and insuring of property, by a title guaranty company, is not practicing law.³⁷ The act of a trust company in giving free advice as to making of wills, where it employed attorneys to draw up such wills at its expense, is "practicing law" within the New York statute forbidding corporations to practice law.³⁸ The right of a guaranty company to enforce an obligation to protect its guaranty, where necessary to carry on its business, is not engaging in

³¹ Binford v. Boyd, 178 Cal. 458, 174 Pac. 56.

³² Binford v. Boyd, 178 Cal. 458, 174 Pac. 56.

³³ People v. Rodgers, 277 Ill. 151, 115 N. E. 146.

³⁴ What constitutes holding corporation out to be lawfully qualified to practice law, see Creditors' Nat. Clearing House v. Bannwart, 227 Mass. 579, 116 N. E. 886.

³⁵ People v. Purdy, 174 N. Y. App. Div. 702, 162 N. Y. Supp. 56; People v. Purdy, 174 N. Y. App. Div. 694, 162 N. Y. Supp. 70.

The prohibition against corpo-

rations to practice law cannot be evaded by the creation of a corporation to obtain reductions of assessments on realty where necessitating the practice of law. People v. Purdy, 174 N. Y. App. Div. 702, 162 N. Y. Supp. 56.

³⁶ Tanenbaum v. Higgins, 190 N. Y. App. Div. 861, 180 N. Y. Supp. 738.

³⁷ People v. Title Guaranty & Trust Co., 191 N. Y. App. Div. 165, 181 N. Y. Supp. 52.

³⁸ People v. People's Trust Co., 180 N. Y. App. Div. 494, 167 N. Y. Supp. 767.

the practice of law as forbidden by the New York statute.³⁹ A mercantile agency company is engaged in the practice of law where it is no more than a broker soliciting legal business for lawyers who are to become principals in the transaction.⁴⁰

The statute prohibiting corporations from practicing law excepts corporations lawfully examining and insuring titles, but only so far as legal work is in connection with such examination and insurance of titles.⁴¹ A title guaranty and trust company does not render legal services, within a statute making it criminal for corporations to render such services, merely because it prepares a bill of sale and chattel mortgage by filling out blanks upon and in accordance with the specific direction of a purported customer. By so holding the court of appeals reversed the decision of the appellate division which had held that the New York statute making it criminal for a corporation to practice law or render "legal services of any kind" covers the act of a title guaranty and trust company in drawing a bill of sale and mortgage, on the theory that "legal services" is not confined to services connected with litigation.⁴²

The fact that a corporation has no authority to practice law does not, it seems, authorize the denial of relief in a certiorari proceeding to review a tax assessment brought by such corporation as attorney for the property owner.⁴³

§ 822. — Practice of dentistry. Prior to 1916, a corporation could not practice dentistry in New York.⁴⁴

³⁹ *In re Kelsey*, 186 N. Y. App. Div. 95, 173 N. Y. Supp. 860.

⁴⁰ *State ex rel. Lundin v. Merchants' Protective Corporation*, 105 Wash. 12, 177 Pac. 694.

⁴¹ *People v. Title Guaranty & Trust Co.*, 180 N. Y. App. Div. 648, 168 N. Y. Supp. 278, rev'd on other grounds in 227 N. Y. 366, 125 N. E. 666.

⁴² *People v. Title Guaranty & Trust Co.*, 227 N. Y. 366, 125 N. E. 666, rev'g 180 N. Y. App. Div. 648, 168 N. Y. Supp. 278.

⁴³ *People ex rel. Floersheimer v.*

Purdy, 221 N. Y. 481, 483, 116 N. E. 390, rev'g 174 N. Y. App. Div. 694, 162 N. Y. Supp. 70.

⁴⁴ *Lewis v. Woodbury Dental Parlors Co.*, 106 N. Y. Misc. 78, 175 N. Y. Supp. 269.

In New York, while a corporation cannot be created to practice dentistry, yet dental corporations created prior to 1916 may, by statute, continue to exist. In *re Lewis v. Harlem Dental Co.*, 189 N. Y. App. Div. 359, 178 N. Y. Supp. 533.

§ 823. Compromise. A lumber company has no power to compromise suits filed against its employees as individuals.⁴⁵

§ 824. Control by or of other corporations.⁴⁶

§ 826. Discontinuance of business by public service corporation.⁴⁷ A purchaser of a railroad at judicial sale or otherwise cannot operate it for its own private purpose or for the purpose of those with whom it may privately contract, to the exclusion of the public.⁴⁸

§ 827. Discriminations. Public service corporations must not unjustly discriminate between patrons.⁴⁹

§ 828. Engaging in different kind of business.⁵⁰

§ 829. Entries on public lands. Under federal statutes limiting entries on coal land to one entry by a person or association of persons, a corporation which has received the benefit of an entry by an individual cannot itself make another such entry.⁵¹

§ 831. Establishment of offices.⁵² It is not ultra vires for a corporation to move its principal place of business from one city to another, or to agree to return money subscribed for stock in case of a failure to make an agreed change.⁵³ The South Dakota statute providing that corporations having a business office outside the state must have their main office for the transaction of business within the state, includes domestic corporations transacting business wholly outside of the state.⁵⁴

⁴⁵ *Rasnick v. W. M. Ritter Lumber Co.*, 187 Ky. 523, 219 S. W. 801.

⁴⁶ See § 804, *supra*, and § 840, *infra*.

⁴⁷ See §§ 4423, 4438, *infra*.

⁴⁸ *Marietta & V. R. Co. v. Public Utilities Commission*, — Ohio St. —, 126 N. E. 889.

⁴⁹ *Homestead Co. v. Des Moines Elec. Co.*, 248 Fed. 439.

Electricity cannot be refused a customer at his place of business

because he refuses to pay for overdue service at his residence. *Merrill v. Livermore Falls Light & Power Co.*, 117 Me. 532, 105 Atl. 120.

⁵⁰ See § 861, *infra*.

⁵¹ *Union Coal & Coke Co. v. United States*, 247 Fed. 106.

⁵² See also § 900, *infra*.

⁵³ *Gasser v. Great Northern Ins. Co.*, — Minn. —, 176 N. W. 484.

⁵⁴ *State v. Public Drug Co.*, 41 S. D. 287, 170 N. W. 161.

§ 832. Furnishing physician to members.⁵⁵ A corporation engaged in the operation of a sawmill has power to employ a physician to look after the health of the employees.⁵⁶

§ 833. Hospitals.⁵⁷

§ 835. Insurance. Charter power of a bank to act as agent for fire insurance companies does not confer authority to itself to insure against fire or to agree to procure insurance.⁵⁸

§ 839. Liquor licenses and sale of liquor. An incorporated golf club has power to dispense liquor to its members and guests, subject to any penal laws.⁵⁹

§ 840. Organization of subsidiary companies. Organization of a selling company, by a coal company, where not for the purpose of preventing competition, is not unlawful.⁶⁰ However, an incorporated college has no power to create a separate institution of learning.⁶¹

§ 841. Partnership—General rules. Except where authorized by statute,⁶² a corporation cannot become a partner in a firm.⁶³ So a corporation cannot become a partner with an individual even if he owns most of the corporate stock.⁶⁴ However, "whether a corporation may become a technical partner

⁵⁵ See also § 886, *infra*.

⁵⁶ *Jackson Lumber Co. v. Trammell*, 199 Ala. 536, 74 So. 469.

⁵⁷ For a note on the subject of "Right of business corporation to use its funds or property for humanitarian purposes," see 3 A. L. R. 443.

⁵⁸ *Alabama Red Cedar Co. v. Tennessee Valley Bank*, 200 Ala. 622, 76 So. 980.

⁵⁹ *Country Club v. State*, — Tex. —, 214 S. W. 296, *aff'd* State v. Country Club, — Tex. Civ. App. —, 173 S. W. 570.

⁶⁰ *Thurmond v. Paragon Colliery Co.*, 82 W. Va. 49, 95 S. E. 816.

⁶¹ *Dubuque German College & Seminary v. St. Joseph's College*, — Iowa —, 169 N. W. 405.

⁶² In Hawaii the statute expressly permits corporations to form a partnership. *Haiku Sugar Co. v. Johnstone*, 249 Fed. 103.

⁶³ *Cole v. Rome Sav. Bank*, 96 N. Y. Misc. 188, 161 N. Y. Supp. 15; *Planters' Oil Co. v. Gresham*, — Tex. Civ. App. —, 202 S. W. 145.

⁶⁴ *Vineyard v. Miller Land Co.*, — Tex. Civ. App. —, 209 S. W. 693.

or not, there is no doubt of its capacity to enter into commercial ventures within the general scope of its corporate powers, whereby the profits or losses of the enterprise are to be divided between the corporation and another person or corporation.”⁶⁵

A partnership formed by corporations is not itself a corporation.⁶⁶

§ 842. — What constitutes partnership.⁶⁷

§ 843. — Exceptions to rule. A corporation is liable on a partnership debt although the partnership agreement was ultra vires, and the other partner cannot set up ultra vires as to the corporation as a defense.⁶⁸ A corporation contributing a place of business, advertising, etc., to a business conducted by an individual, for a share of the profits, cannot escape liability for negligence of the individual in conducting the business.⁶⁹

§ 847. Speculations on stock or grain market. A bank has no power to engage in buying and selling cotton for future delivery.⁷⁰ A cotton oil company incorporated to manufacture cotton seed oil and products and gin cotton, “with power to purchase, or construct and maintain mills and gins for such purpose, and with power to purchase such goods, wares and merchandise used for such business,” has no power to buy and sell baled cotton for speculation.⁷¹

§ 848. Taking and enforcing securities.⁷²

§ 855. Utilization of surplus or idle property. A corporation created to maintain cotton seed oil mills, and to sell cotton

⁶⁵ Clinchfield Fuel Co. v. Henderson Iron Works Co., 254 Fed. 411, 415.

⁶⁶ Haiku Sugar Co. v. Johnstone, 249 Fed. 103.

⁶⁷ Whether corporation a partner in particular case, see Fink v. Brown, — Tex. —, 215 S. W. 846.

What constitutes partnership between bank and another, see Cole v. Rome Sav. Bank, 96 N. Y. Misc. 188, 161 N. Y. Supp. 15.

⁶⁸ Hayes-Thomas Grain Co. v. A. F. Wilcox Contracting Co., — Ark. —, 223 S. W. 357.

⁶⁹ Cassut v. George W. Miller Co., 103 Wash. 222, 174 Pac. 433.

⁷⁰ Martin v. Hemphill, — Tex. Civ. App. —, 221 S. W. 333.

⁷¹ Planters' Cotton Oil Co. v. Guaranty State Bank, — Tex. Civ. App. —, 188 S. W. 38.

⁷² Power to make loans generally, see §§ 946-949, *infra*.

seed and by-products, has power to purchase cattle to be fed on hulls, where there was no market for such hulls.⁷³ Where a corporation had power to acquire a tug in discharge of a debt due it, it had power to contract for its use to make it profitable.⁷⁴ A brewing company, whose charter is very broad, and which has constructed a dumping board on its water front, has power to use the dumping board so as to gain an income from it, by hiring scows in which refuse could be dumped and hiring tugs to move the scows.⁷⁵

In Pennsylvania, however, a railroad company operated by electricity and having a plant of its own for the development of electric power, has no power to sell surplus power to an independent coal company, since by so doing it would engage in another business.⁷⁶

III. PARTICULAR CORPORATIONS

§ 857. Agricultural societies. A mutual co-operative corporation, created other than for pecuniary profit, has power to fix a charge of three per cent on gross sales of produce of its members, whether sold through the corporation or otherwise.⁷⁷

§ 859. Banks—In general. A bank empowered “to act as agent for fire insurance” companies has no authority to insure property.⁷⁸ A bank does not violate a statute prohibiting banks from going into trade or commerce “by buying or selling goods,” etc., merely because it buys a draft with bill of lading attached and indorses such draft.⁷⁹ A bank may agree to honor overdrafts for a customer.⁸⁰

⁷³ Hollis Cotton Oil, Light & Ice Co. v. Marrs & Lake, — Tex. Civ. App. —, 207 S. W. 367.

⁷⁴ Clinchfield Fuel Co. v. Henderson Iron Works Co., 254 Fed. 411.

⁷⁵ C. F. Harms Co. v. Leonhard Michel Brewing Co., 228 N. Y. 263, 126 N. E. 705, rev'g 183 N. Y. App. Div. 886, 169 N. Y. Supp. 1088.

⁷⁶ Citizens' Elec. Illuminating Co. v. Lackawanna & W. V. Power

Co., 255 Pa. 176, 99 Atl. 465.

⁷⁷ Ex parte Baldwin County Producers' Corporation, — Ala. —, 83 So. 69.

⁷⁸ Alabama Red Cedar Co. v. Tennessee Valley Bank, 200 Ala. 622, 76 So. 980.

⁷⁹ Marsh Milling & Grain Co. v. Guaranty State Bank, — Okla. —, 171 Pac. 1122.

⁸⁰ Saylor v. State Bank of Allen, 99 Kan. 515, 163 Pac. 454.

A national bank cannot engage in the business of buying and selling cotton⁸¹ or cattle,⁸² and has no power to negotiate loans for others,⁸³ or to contract to loan money belonging to a depositor.⁸⁴ On the other hand, it has power to establish a pension fund for employees.⁸⁵

Powers conferred on national banks by the federal government cannot be impaired by a state.⁸⁶ Under the Federal Reserve Act, national banks have all the powers granted by state laws to state banks, and a state cannot forbid the exercise by national banks of powers conferred by it on state banks.⁸⁷

§ 860. — Power to act as depository. A national bank has power to accept a special deposit of valuable securities.⁸⁸

§ 861. — Engaging in other business to save debt. A national bank which has bought in a street railway to protect its debt has no power to operate the road, or at least is under no duty to operate it.⁸⁹

§ 862. Brewing companies.⁹⁰

§ 863. Building and loan associations.⁹¹ The obtaining of fire insurance for a member is an incidental power of a building and loan association, in connection with its loans.⁹²

⁸¹ First Nat. Bank v. McKown, — Okla. —, 176 Pac. 245.

⁸² First Nat. Bank v. Stokes, 134 Ark. 368, 203 S. W. 1026.

⁸³ Pollock v. Lumbermen's Nat. Bank, 86 Ore. 324, L. R. A. 1918 B 402, 168 Pac. 616.

⁸⁴ Holmes v. Uvalde Nat. Bank, — Tex. Civ. App. —, 222 S. W. 640.

⁸⁵ Heinz v. National Bank of Commerce, 237 Fed. 942, 952.

⁸⁶ Fidelity Nat. Bank & Trust Co. of Kansas City v. Enright, 264 Fed. 236.

⁸⁷ Hamilton v. State, — Conn. —, 110 Atl. 5'

⁸⁸ Security Nat. Bank v. Home Nat. Bank, 106 Kan. 303, 187 Pac. 697.

⁸⁹ A national bank may set up the defense of ultra vires where it is sought to compel it to operate a railway which it bought. Gress v. Ft. Loramie, 100 Ohio St. 35, 125 N. E. 112.

⁹⁰ See § 855, supra.

⁹¹ Power to issue bonds. see § 971, infra.

⁹² Biggs v. Carbondale Building Loan & Homestead Ass'n, 194 Ill. App. 171.

§ 864. **Canal companies.** That a canal company not authorized by its charter to charge toll, has no power to make such charge, is well settled.⁹³

§ 865. **Cemetery companies.**⁹⁴

§ 866. **Charitable corporations.** Money derived from pay patients cannot be diverted to private profit by a hospital which is a charitable corporation.⁹⁵

§ 867. **Colleges and universities.**⁹⁶

§ 873. **Land and investment companies.** The power of land companies is not limited to the accomplishment of any specific enterprise.⁹⁷

§ 876. **Manufacturing companies.** A company created to manufacture automobiles has power to smelt ore for its own uses.⁹⁸

§ 880. **Public service companies in general.**⁹⁹ A corporation of a public nature cannot so deal with its property as either to incapacitate itself from performing or from fettering itself in the full performance of its public duties.¹ Power to conduct a ferry includes power to provide approaches.²

§ 882. **Railroads—In general.**³ The powers of railroad companies are defined by special statutes in most states, at least to

⁹³ *Forbes Pioneer Boat Line v. Board of Commissioners*, — Fla. —, 82 So. 346.

⁹⁴ See *In re Chauncey*, 191 N. Y. App. Div. 359, 181 N. Y. Supp. 653; *Baylis v. Van Nostrand*, 176 N. Y. App. Div. 396, 162 N. Y. Supp. 831.

⁹⁵ *O'Brien v. Physicians' Hospital Ass'n*, 96 Ohio St. 1, L. R. A. 1917 F 741, 116 N. E. 975.

⁹⁶ Power to accept bequests, see § 1073, *infra*.

⁹⁷ *Miller v. Herzberg*, 202 Ala. 613, 81 So. 555.

⁹⁸ *Dodge v. Ford Motor Co.*, 204 Mich. 459, 170 N. W. 668.

⁹⁹ Powers of particular power company, as to appropriating water, see *East Hartford Fire Dist. v. Glastonbury Power Co.*, 92 Conn. 217, 102 Atl. 592.

¹ *County Hotel & Wine Co., Ltd. v. London & N. W. Ry. Co.*, [1918] 2 K. B. 251, 266.

² *Hart v. King County*, 104 Wash. 485, 177 Pac. 344.

³ Sale of surplus power, see § 855, *supra*.

Incidental powers of railroad

some extent.⁴ So long as a railroad company holds lands in fee, for a right of way, it may bore oil wells and take oil therefrom.⁵ A railroad company, to advertise lands along its route to bring settlers, has power to agree to pay a reasonable commission on sales of such lands to settlers, although it does not own such lands.⁶ It has also been held, however, that the promotion of town building, to increase business, is not within the powers of a railroad company.⁷

§ 883. — Location of road.⁸ A railroad company has no power to abandon and change its location, without statutory authority.⁹ A franchise to construct its road along streets does not authorize a railroad company to construct industrial spur tracks.¹⁰

§ 885. — Refreshment houses, dining cars, hotels and Y. M. C. A. A railroad company cannot contract so as to deprive itself of the use and occupation of its own refreshment rooms at a station in a large junction point, and inflict upon itself a lasting inability to supply food to passengers at such station.¹¹

§ 895. Trust companies. Trust companies doing a banking business may certify checks.¹² In Missouri, they may receive deposits and acquire negotiable paper.¹³ A trust company authorized to act as trustee to hold title to a spendthrift trust

companies in general, review of English decisions see *County Hotel & Wine Co., Ltd. v. London & N. W. Ry. Co.*, [1918] 2 K. B. 251, 267-271.

⁴ See *Gulf Pipe Line Co. v. Lasater*, — Tex. Civ. App. —, 193 S. W. 773.

⁵ *Crowell & Conner v. Howard*, — Tex. Civ. App. —, 200 S. W. 911.

⁶ *Thrailkill v. Crosbyton-South-plains R. Co.*, 246 Fed. 687, L. R. A. 1918 C 90.

⁷ *Foster Lumber Co. v. Atchison, T. & S. F. R. Co.*, 270 Mo. 629,

L. R. A. 1918 A 768, 194 S. W. 281.

⁸ See also § 1173, *infra*.

⁹ *Jeff Bland Lumber & Building Co. v. Railroad Commission*, — Tex. Civ. App. —, 203 S. W. 402.

¹⁰ *Simons Brick Co. v. City of Los Angeles*, — Cal. —, 187 Pac. 1066.

¹¹ *County Hotel & Wine Co., Ltd. v. London & N. W. Ry. Co.*, [1918] 2 K. B. 251.

¹² *State v. Scarlett*, 91 N. J. L. 200, 2 A. L. R. 83, 102 Atl. 160.

¹³ *Denny v. Jefferson County*, 272 Mo. 436, 199 S. W. 250.

fund has the same powers as trustee that an individual trustee would have.¹⁴

§ 898. Water companies.¹⁵ A "water company may lawfully carry on at the same time two or more separate and distinct systems of public service in different places, or for different uses in the same territory."¹⁶

¹⁴ *Kerens v. St. Louis Union Trust Co.*, — Mo. —, 223 S. W. 645.

¹⁵ Water companies, powers and rights as to water power, see

Cuyahoga River Power Co. v. Northern Ohio Traction & Light Co., 252 U. S. 388, 64 L. Ed. 626.

¹⁶ *Riverside Land Co. v. Jarvis*, 174 Cal. 316, 163 Pac. 54.

CHAPTER 22

CONTRACTS IN GENERAL

§ 900. General rule.

§ 901. Contracts foreign to objects for which corporation created—General rule.

§ 902. — Contracts beneficial to corporation.

§ 905. Illegal contracts—Contracts prohibited by charter or statute.

§ 906. — Contracts against public policy.

§ 908. Contracts as binding on other corporations.

§ 911. Assumption of pre-existing debts.

§ 914. Contracts by quasi public corporations.

§ 915. Employment of agents, attorneys and servants.

§ 916. Implied contracts.

§ 918. Limitation of indebtedness—Increase in indebtedness.

§ 920. — Mere change in form of indebtedness.

§ 921. Construction of contracts.

§ 922. Presumptions and evidence.

§ 900. General rule. A corporation may enter into a contract of bailment,¹ and a bank has power to contract for the sawing of lumber taken for a debt.² Of course a corporation has power to agree to repay money delivered to it by another and claimed by third persons, in case it should be determined that such third persons are in law entitled thereto.³

Power to contract, as granted by statute in Canada, is not taken away by statements in the charter defining the objects of incorporation nor even by express restrictions in the charter.⁴

§ 901. Contracts foreign to objects for which corporation created—General rule. A contract is invalid, ordinarily, where relating to a business other than the one for which the company was incorporated.⁵

¹ Arthur Wagner Co. v. Gal-
laher & Speck, 204 Ill. App. 206.

² Paterson & Edey Lumber Co.
v. Bank of Mobile, — Ala. —, 84
So. 721.

³ Eddleman v. Wafford, — Tex.
Civ. App. —, 217 S. W. 221.

⁴ Edwards v. Blackmore, 42
Dom. L. Rep. (Can.) 280.

⁵ Orpheum Theatre & Realty

§ 902. — **Contracts beneficial to corporation.** A railroad company, owning the controlling interest in another railroad company, has authority to agree to buy the notes of the subsidiary for a period of years in such amounts as may be necessary to pay interest on the bonds of the subsidiary; and the contract, made with the trustee for the bondholders, is not discharged by the subsequent insolvency of the subsidiary.⁶

§ 905. **Illegal contracts—Contracts prohibited by charter or statute.** Any contract by a public service corporation to furnish service is invalid where in violation of the Public Utilities Act.⁷ A contract by which a power company agreed to perpetually furnish specified power to a manufacturing company, in consideration of a transfer of power created by the dam of the latter, is not invalid as a contract to furnish power at a less rate than the schedule of charges approved by the Public Utilities Act.⁸

§ 906. — **Contracts against public policy.** Contracts with a public service company tending to stifle competition are void.⁹ A contract by which a manufacturing company transferred to a power company power created by its dam under an agreement by the latter to perpetually furnish the former certain specified power, is not invalid as against public policy.¹⁰

§ 908. **Contracts as binding on other corporations.**¹¹ A dominating corporation is liable for the debts of its dummy, where the one corporation controls the other, as where one corporation was organized to be financed by another.¹² However, corporations, like individual stockholders, are distinct entities and one cannot be treated as the "alter ego" or agent of the other

Co. v. Seavey & F. Brokerage Co., 197 Mo. App. 661, 199 S. W. 257.

⁶ Equitable Trust Co. v. Denver & R. G. R. Co., 250 Fed. 327.

⁷ Schiller Piano Co. v. Illinois Northern Utilities Co., 288 Ill. 580, 123 N. E. 631.

⁸ Schiller Piano Co. v. Illinois Northern Utilities Co., 288 Ill. 580, 123 N. E. 631.

⁹ Coombs v. Burk, — Cal. App. —, 180 Pac. 59.

¹⁰ Schiller Piano Co. v. Illinois Northern Utilities Co., 288 Ill. 580, 123 N. E. 631.

¹¹ See also § 22 et seq., supra.

¹² Dillard & Coffin Co. v. Richmond Cotton Oil Co., 140 Tenn. 290, 204 S. W. 758.

when openly contracting for itself and in its own corporate name.¹³ Two or more corporations who cause to be organized in another state a new corporation which makes a contract to construct a railroad, are not liable on the contract although the former control the stock and the principal officers of the contracting corporation, and "the identity of stockholders and the control of the contract corporation does not operate to merge the corporations into one or make either the agent of the other."¹⁴ Where a corporation is a large creditor of another company, the fact that it takes an active part in the management of the latter to protect its debt does not make it liable for the debts of the debtor company.¹⁵ The fact that a coal company was organized and at all times managed and controlled by a railroad company as an adjunct to or agency of the railroad company for the operation of the coal property operated by it does not make the railroad company liable on the bonds of the coal company.¹⁶ Operation by one company of a business formerly belonging to another company does not render the company in possession liable for damages growing out of a breach of contract entered into by the other company.¹⁷

The state is not liable for services rendered to a state hospital although the hospital is not self-sustaining and the state actually supports it and eventually has to pay its debts.¹⁸

§ 911. Assumption of pre-existing debts. A corporation which purchases property may assume debts connected with the property.¹⁹

§ 914. Contracts by quasi public corporations.²⁰ A public service company, such as a railroad company, cannot contract

¹³ *Marsch v. Southern New England R. Corporation*, 230 Mass. 483, 120 N. E. 120, and see § 45, *supra*.

¹⁴ *Marsch v. Southern New England R. Corporation*, 230 Mass. 483, 120 N. E. 120.

¹⁵ *Chicago Mill & Lumber Co. v. Boatmen's Bank*, 234 Fed. 41.

¹⁶ *New York Trust Co. v. Carpenter*, 250 Fed. 668.

¹⁷ *McAlister v. American Ry.*

Express Co., 179 N. C. 556, 103 S. E. 129.

¹⁸ *Watkins Boating Co. v. State*, 106 N. Y. Misc. 693, 175 N. Y. Supp. 310.

¹⁹ *Western Nat. Bank v. Wittman*, 31 Cal. App. 615, 161 Pac. 137.

²⁰ Extent of power of irrigation company to contract as to water supply, see *Northern Irrigation Co. v. Watkins*, — Tex. Civ. App. —, 183 S. W. 431.

to relieve itself from the diligent performance of those duties to the public which the law imposes on it.²¹ On the other hand, a railroad company, when not contracting in its character of common carrier, has the same right to contract as other corporations.²²

§ 915. Employment of agents, attorneys and servants.²³

Under a statute giving corporations the power to remove servants "at will," corporations have no power to make a contract for permanent employment.²⁴ Where a contract for services of an attorney for a fixed term provided for its termination if the services should not be satisfactory to the board of directors but that the board should not so vote until after a hearing at a meeting "upon the cause or reason of such termination," the contract could not be terminated without substantial cause.²⁵

§ 916. Implied contracts. Corporations, like individuals, may be held upon an implied promise.²⁶ For instance, a corporation is liable on implied contract for services accepted by the corporation.²⁷ So a corporation is liable, on an implied contract, for the value of goods converted by a branch manager and which he could have purchased, where used in the business.²⁸

§ 918. Limitation of indebtedness—Increase in indebtedness.²⁹ A guaranty by one company of the bonds of another is not an increase of "bonded indebtedness" as used in the constitution and statutes.³⁰

²¹ *Hearn v. Central of Georgia R. Co.*, 22 Ga. App. 1, 95 S. E. 368.

²² *Hicks v. Gulf, C. & S. F. Ry. Co.*, — Tex. Civ. App. —, 212 S. W. 840.

²³ See also § 1767, *infra*.

A corporate contract allowing brokers commissions of \$1,800,000 for selling property for \$5,800,000 is so unconscionable as to be unenforceable. *Bassick v. Aetna Explosives Co.*, 246 Fed. 974, 993.

²⁴ *Williams v. Great Northern R. Co.*, 108 Wash. 344, 184 Pac. 340.

²⁵ *Gilman v. Lamson Co.*, 234 Fed. 507.

²⁶ *Cochrane v. Interstate Packing Co.*, 139 Minn. 452, 167 N. W. 111.

²⁷ *Hopkins v. Paradise Heights Fruit Growers' Ass'n*, — Mont. —, 193 Pac. 389.

²⁸ *Wentworth v. Winton Co.*, 97 Ore. 541, 188 Pac. 204.

²⁹ See also § 979, *infra*.

³⁰ *Bank of Newman v. Monterey County Gas & Electric Co.*, — Cal. App. —, 191 Pac. 970.

§ 920. — **Mere change in form of indebtedness.** Debt limit provisions apply only to new debts and not, it seems, to renewals of old debts.³¹ Where a corporation had authority to purchase bonds, its own bonds issued to take up the notes given for the bonds previously purchased do not constitute an increase of indebtedness.³²

§ 921. **Construction of contracts.** In construing a resolution of a board of directors, the intent must be gathered from the reading of the resolution interpreted in the light of the circumstances and reasons existing for it at the time.³³

§ 922. **Presumptions and evidence.** It is presumed that a contract is within the powers of the corporation where nothing appears to the contrary.³⁴

³¹ *Parsons v. Rinard Grain Co.*, citing *Fletcher Cyc. Corp.* § 921. — *Iowa* —, 173 N. W. 276.

³² *Wrightsville Hardware Co. v. McElroy*, 254 Pa. 422, 98 Atl. 1052.

³³ *Copper King Min. Co. v. Hanson*, — *Utah* —, 176 Pac. 623, citing *Alabama City, G. & A. R. Co. v. Kyle*, 202 Ala. 552, 81 So. 54; *Chesapeake Beach Ry. Co. v. Hupp Automatic Mail Exchange Co.*, 48 App. Cas. (D. C.) 123.

CHAPTER 23

POWERS AS TO SURETYSHIP AND GUARANTY

I. EXPRESS POWER

§ 923. Nature and extent.

II. IMPLIED POWER

§ 924. General rule.

§ 925. Applicability of rule to particular corporations.

§ 926. Where in furtherance of business—General rule.

§ 927. — As part of business.

§ 928. — For purpose of transfer of corporate property.

§ 929. — To protect indebtedness or pay debt.

§ 930. — To increase business.

I. EXPRESS POWER

§ 923. Nature and extent.¹ Power of certain corporations to become sureties on bonds is often expressly conferred by statute.² Express power to act as surety on bail bonds includes power to agree to indemnify a surety on a bail bond, since the character of instrument which it employs to bind itself is immaterial.³

In Texas it is held that a surety company is governed by the same rules as to liability as determines the liability of uncompensated sureties.⁴ In some other states, surety corporations are not entitled to the favor shown sureties generally; and their contracts will be construed most favorably to the obligee there-

¹ Powers of surety company, see *Denecke v. West*, 184 Iowa 600, 169 N. W. 97.

² *Wells v. Fidelity & Deposit Co.*, 146 La. 169, 83 So. 448.

³ *Texas Fidelity & Bonding Co. v. General Bonding & Casualty Ins. Co.*, — Tex. —, 216 S. W.

144, holding also that express power to guarantee contracts or undertakings of others included such power.

⁴ *Hess & Skinner Engineering Co. v. Turney*, — Tex. —, 216 S. W. 621, aff'g — Tex. Civ. App. —, 207 S. W. 171.

in.⁵ In Pennsylvania it is held that a surety company has not the same defenses as an individual surety, and is not discharged by a mere change in the contract as in case of an ordinary suretyship.⁶

II. IMPLIED POWER

§ 924. General rule. The general rule is that a corporation has no implied power to guarantee a debt or contract for the sole benefit of another.⁷

§ 925. Applicability of rule to particular corporations. Thus, a construction company has no authority to contract to indemnify a surety company against loss as a surety on a bond, where not incidental to the conduct of its business.⁸ So a company created to conduct a mercantile business has no authority to pledge its assets to pay debts other than its own, by an agreement to pool its earnings with certain insolvent corporations.⁹ It is said that "a transportation corporation cannot contract as an insurance company because the statute expressly authorizes insurance corporations." This was said in connection with a claim of an employee against a railroad company for indemnity for amount spent for medical treatment and hospital charges.¹⁰

A bank cannot guarantee individual contracts of its cashier,¹¹ nor the debt of a drug company for rent,¹² nor the note of another except where necessary to dispose of its own paper.¹³

⁵ Board of Com'rs of Ohio v. Clemens, — W. Va. —, 100 S. E. 680.

⁶ Philadelphia v. Ray, — Pa. —, 109 Atl. 689.

⁷ Miller v. Northern Brewery Co., 242 Fed. 164; First Nat. Bank v. Towner, 239 Fed. 433; Ingram v. Texas Christian University, — Tex. Civ. App. —, 196 S. W. 608.

A pledge of the credit of a corporation to promote the business of another company, where not beneficial, is beyond the power of a corporation. Stone-Ordean-Wells Co. v. New England Pie Co., 201 Mich. 407, 167 N. W. 943.

⁸ United States Fidelity & Guaranty Co. v. Cascade Const. Co., 106 Wash. 478, 180 Pac. 463.

⁹ Kaplan Dry Goods Co. v. Sanger Bros., — Tex. Civ. App. —, 214 S. W. 485.

¹⁰ Gulf, C. & S. F. Ry. Co. v. Goodman, — Tex. Civ. App. —, 189 S. W. 326.

¹¹ Brown v. Bank of Covington, — Ga. App. —, 101 S. E. 196.

¹² Tracy Loan & Trust Co. v. Merchants Bank, 50 Utah 196, 167 Pac. 353.

¹³ International Harvester Co. v. State Bank, 38 N. D. 632, 166 N. W. 507.

Banks, either national or state, have no power to assume the liabilities of an insolvent state bank in the city.¹⁴ A national bank has no power to guarantee the payment or performance of the obligations of others for their benefit.¹⁵

§ 926. Where in furtherance of business—General rule. In some cases, "one corporation may lawfully give security for the debt of another."¹⁶ Thus, a bank may, under certain circumstances, enter into a contract of guaranty.¹⁷ For instance, a bank which leases offices to a city has power to agree to indemnify the city against liability to another for rental of other offices by holding over.¹⁸ A corporation may guarantee payment of a note where it receives a direct benefit therefrom.¹⁹ A brick company has power to agree to indemnify a railroad from liability for negligence in the construction or operation of a spur track running to the brick plant.²⁰

The "Liability of national bank on guaranty of loan to third person from which it derives benefit" is the subject of a late note in the American Law Reports.²¹

§ 927. — As part of business. A corporation may guarantee debts of another for which it is primarily liable.²² Thus, a national bank may guarantee payment of a loan to a third person where the loan in fact went to the corporation.²³ So a bank

¹⁴ Board of Com'rs v. Citizens' Trust & Savings Bank, — Ind. App. —, 123 N. E. 130.

¹⁵ Rice & Hutchins Atlanta Co. v. Commercial Nat. Bank of Macon, 18 Ga. App. 151, 88 S. E. 999; First Nat. Bank v. Crespi & Co., — Tex. Civ. App. —, 217 S. W. 705; Farmers' & Merchants' Bank of Reedsville v. Kingwood Nat. Bank, — W. Va. —, 101 S. E. 734.

¹⁶ Gigoux v. Moore, 105 Kan. 361, 184 Pac. 637.

¹⁷ Eckhart v. Heier, 38 S. D. 524, 162 N. W. 150.

¹⁸ Voelcker v. Schnell, 166 N. Y. Supp. 420.

¹⁹ Parlin & Orendorff Improve-

ment Co. v. Frey, — Tex. Civ. App. —, 200 S. W. 1143.

²⁰ Houston & T. C. R. Co. v. Diamond Press Brick Co., — Tex. —, 222 S. W. 204, rev'g — Tex. Civ. App. —, 188 S. W. 32.

²¹ 6 A. L. R. 172, annotating Ellis v. Citizens' Nat. Bank, 25 N. M. 319, 6 A. L. R. 166, 183 Pac. 34.

²² C. F. Harms Co. v. Leonhard Michel Brewing Co., 228 N. Y. 263, 126 N. E. 705, rev'g 183 N. Y. App. Div. 886, 169 N. Y. Supp. 1088.

²³ Ellis v. Citizens' Nat. Bank, 25 N. M. 319, 6 A. L. R. 166, 183 Pac. 34.

has power to guarantee payment of an account by a customer where incidental to a loan by the bank to such customer.²⁴ A national bank has power to guarantee checks drawn thereon by one person payable to another in connection with a transaction in the course of its business, where it had possession of property of the drawer of the check, where in effect an agreement to pay one out of the proceeds of his own property.²⁵ A corporation chartered to engage in the wholesale and retail implement, vehicle and merchandise business has power to act as sales agent of implements and guarantee the payment of notes given by a purchaser thereof.²⁶ A university has power to contract for the rent of a building for a medical college which was a correlated school, since the building up of one department tends to promote the welfare and growth of the university as a whole.²⁷ Where guaranties of debts of licensees by a corporation were to prevent business coming to a standstill, they are authorized.²⁸

A new phase of the question is presented by a holding that a corporation has implied power to guarantee payment by a salesman of the company for furniture he proposed to buy, to prevent the salesman quitting his job, where the salesman was a valuable man and had several prospects which might net him large commissions.²⁹

§ 928. — For purpose of transfer of corporate property.³⁰

Power of a land company to sell land includes power to execute an indemnity covenant in connection with such a sale.³¹ In selling undisposed of stock in the treasury, a corporation has power to guarantee to furnish a buyer within a specified time at a profit to the original purchaser.³²

²⁴ *J. L. Mott Iron Works v. Kaiser Co.*, — S. C. —, 103 S. E. 783. *Pavement Co.*, 227 Mass. 206, 116 N. E. 266.

²⁵ *Armstrong v. First Nat. Bank*, — Mo. App. —, 195 S. W. 562.

²⁶ *Advance Rumely Thresher Co. v. Evans Metcalf Implement Co.*, 103 Kan. 532, 175 Pac. 392.

²⁷ *Ingram v. Texas Christian University*, — Tex. Civ. App. —, 196 S. W. 608.

²⁸ *Edwards v. International*

²⁹ *M. Burg & Sons v. Twin City Four Wheel Drive Co.*, 140 Minn. 101, 167 N. W. 300.

³⁰ See also § 604, *supra*.

On sale of bonds, see § 1029, *infra*.

³¹ *National Land & Loan Co. v. Rat Portage Lumber Co.*, 36 Dom. L. Rep. (Can.) 97.

³² *Lemmon v. East Palestine*

§ 929. — To protect indebtedness or pay debt. Where a customer of a corporation was in its debt to a considerable amount, which debt would be a total loss if aid was not extended him, the corporation has power to guarantee payment by the customer for goods purchased from another company.³³ A national bank, as an unsecured creditor of one practically without assets except an uncompleted government contract, has power to join in a bond of indemnity to enable trustees in bankruptcy of the debtor to complete the contract.³⁴

§ 930. — To increase business. A corporation may make a contract of guaranty in aid of a customer unless clearly beyond its powers as a matter of law.³⁵ A corporation may guarantee payment of rent by another where it directly enhances its business.³⁶ For instance, a brewing company may guarantee the payment of rent by a customer.³⁷ So a corporation in the business of selling theatrical costumes has power to guarantee a contract by a moving picture company for lumber needed to produce a film, where the guarantor had a pending contract to furnish the costumes for such film.³⁸ In Texas, however, a lumber company has no power to sign a contractor's bond, with the idea of making him a customer.³⁹

Rubber Co., 260 Pa. 28, 103 Atl. 510, and see § 604, *supra*.

³³ *Armour & Co. v. R. Rosenberg & Sons Co.*, 36 Cal. App. 773, 173 Pac. 404.

³⁴ *Second Nat. Bank of Parkersburg v. United States Fidelity & Guaranty Co.*, 266 Fed. 489.

³⁵ *Woods Lumber Co. v. Moore*, — Cal. —, 191 Pac. 905, reviewing at some length the general question.

³⁶ *Weiss v. Fred Bender Store Fixture Co.*, 207 Ill. App. 72.

³⁷ *Miller v. Northern Brewery Co.*, 242 Fed. 164, where lessee agreed that failure to handle the beer of the guaranteeing company should operate as an immediate

assignment and transfer of the lease to it; *James Eva Estate v. Mecca Co.*, — Cal. App. —, 181 Pac. 415; *Halloran v. Jacob Schmidt Brewing Co.*, 137 Minn. 141, L. R. A. 1917 E 777, 162 N. W. 1082; *Depot Realty Syndicate v. Enterprise Brewing Co.*, 87 Ore. 560, L. R. A. 1918 C 1001 with note, 170 Pac. 294, at least where customer agrees to handle the products of such brewer exclusively.

³⁸ *Woods Lumber Co. v. Moore*, — Cal. —, 191 Pac. 905.

³⁹ *W. C. Bowman Lumber Co. v. Pierson*, — Tex. —, 221 S. W. 930.

CHAPTER 24

POWER TO ACT IN A REPRESENTATIVE OR FIDUCIARY CAPACITY

§ 932. Power to act as agent or attorney in fact.

§ 933. Power to act as trustee.

§ 937. Power to act as executor or administrator.

§ 932. Power to act as agent or attorney in fact. A corporation may act as the agent of another corporation unless prohibited by its charter.¹ A trust company authorized to act as agent may buy corporate stock for a client although it has no power to purchase it for itself.² A corporation may be the agent of another corporation for the purpose of service of process.³

§ 933. Power to act as trustee.⁴ A charitable bequest may be made to a corporation in trust.⁵

National banks may act as trustees, etc., where no state law is contravened.⁶ The provision of the act establishing the Federal Reserve Board authorizing it to grant permits to national banks to act as trustee, executor, etc., is a valid exercise of the power of Congress.⁷

§ 937. Power to act as executor or administrator.⁸ Except as authorized by statute, a corporation cannot act as executor

¹ *Alley v. Bessemer Gas Engine Co.*, 262 Fed. 94.

² *Commercial Bank & Trust Co. v. Beach*, — Colo. —, 180 Pac. 982, and see § 1122, *infra*.

³ *Calhoun Mills v. Black Diamond Collieries*, 112 S. C. 332, 99 S. E. 821, and see § 2991 et seq., *infra*.

⁴ Power of legislature to authorize, see § 168, *supra*.

⁵ *Roberts v. Corson*, — N. H. —, 107 Atl. 625.

⁶ *Attorney General ex rel. Union Trust Co. v. First Nat. Bank of Bay City*, 192 Mich. 640, 159 N. W. 335.

⁷ *First Nat. Bank of Bay City v. Fellows ex rel. Union Trust Co.*, 244 U. S. 416, 61 L. Ed. 1233, L. R. A. 1918 C 283, rev'g *Attorney General ex rel. Union Trust Co. v. First Nat. Bank of Bay City*, 192 Mich. 640, 159 N. W. 335.

⁸ See also § 168, *supra*.

or administrator,⁹ although in most states a corporation may now serve as an executor or administrator.¹⁰ However, charter authority of a bank to "accept and hold all such trusts" as may be committed to it does not empower it to act as executor.¹¹ So the word "person" as used in statutes relating to appointment as executor, etc., is often deemed confined to individuals and not to extend to corporations.¹² State law must yield to the federal law authorizing national banks to act as administrator.¹³

⁹ Attorney General ex rel. Union Trust Co. v. First Nat. Bank of Bay City, 192 Mich. 640, 159 N. W. 335.

¹⁰ Equitable Trust Co. v. Plume, 92 Conn. 649, 103 Atl. 940; In re Rath's Estate, 107 N. Y. Misc. 598, 176 N. Y. Supp. 887; Simmons v. Campbell, — Tex. Civ. App. —, 213 S. W. 338.

¹¹ German-American Bank v. Kopp, 132 Md. 422, 103 Atl. 1009.

¹² Attorney General ex rel. Union Trust Co. v. First Nat. Bank of Bay City, 192 Mich. 640, 159 N. W. 335, and see § 54, supra.

¹³ In re Stanchfield's Estate, — Wis. —, 178 N. W. 310.

CHAPTER 25

POWER TO BORROW AND LOAN

I. POWER TO BORROW

§ 940. As dependent on purpose for which borrowed.

§ 941. As dependent on nature and kind of corporation.

§ 943. Extent of power to borrow.

§ 945. Defenses to actions to recover back.

II. POWER TO LOAN

§ 946. Implied power—In general.

§ 947. — To further corporate interests.

§ 949. Constitutional, charter or statutory prohibition or restriction.

I. POWER TO BORROW

§ 940. **As dependent on purpose for which borrowed.** An insurance company has power to borrow money to be spent to acquire new business.¹ A national bank has no power to borrow money, or to guarantee the payment of money borrowed by trustees, for use in the purchase of its stock to be parceled out among employees as a benefit fund.²

§ 941. **As dependent on nature and kind of corporation.** A railroad may borrow money for lawful purposes,³ as may an insurance company.⁴

§ 943. **Extent of power to borrow.** Power to borrow money and incur debts includes power to issue so-called "preferred rights" acknowledging indebtedness and agreeing to pay divi-

¹ Kingston v. Home Life Ins. Co. of America, — Del. Ch. —, 101 Atl. 898.

² Commonwealth Trust Co. v. First-Second Nat. Bank, 260 Pa. 223, 103 Atl. 598.

³ Brown v. Boston & M. R. R., 233 Mass. 428, 124 N. E. 322.

⁴ Royal Bank v. B. C. Accident, 35 Dom. L. Rep. (Can.) 650

dends and interest, although neither capital stock nor an incumbrance on the property.⁵

§ 945. Defenses to actions to recover back. A corporation cannot escape payment of a loan to it because the money did not pass through the hands of the treasurer nor because of the absence of any reference thereto in the corporate minutes.⁶

II. POWER TO LOAN

§ 946. Implied power—In general.⁷ A contract whereby a company advances a fixed per cent of the face value of accounts of another company, to the latter, and on collection returns the balance less expenses and an agreed charge, is a loaning contract and not within the power of a mercantile company incorporated under the general incorporation act of Illinois.⁸ A loan by a bank is not beyond its power merely because its incidental effect is to "float and keep alive" another bank.⁹

§ 947. — To further corporate interests. Loans by a corporation to a licensee, as incidental to and in furtherance of the corporate business, are within the power of a corporation.¹⁰ A brewing company may loan money to a saloon keeper to carry on business, so as to be able to sell beer to him.¹¹ A corporation owning a patent right and holding a portion of the capital stock of another company issued to it in consideration of the right to use such patent, has a right to sell such stock and turn over the proceeds to the operating company to relieve it of financial embarrassment, with the understanding that such proceeds were to be accounted for on a basis thereafter to be determined.¹²

§ 949. Constitutional, charter or statutory prohibition or restriction. A corporation created under the General Incorporation

⁵ *Biel v. Union Fuel & Ice Co.*,
— Wash. —, 177 Pac. 813.

⁶ *Scouton v. Stony Brook Lumber Co.*, 261 Pa. 241, 7 A. L. R. 1433, 104 Atl. 548.

⁷ Power to loan on particular securities, see §§ 848-853, *supra*.

⁸ *National Trust & Credit Co. v. F. H. Orcutt & Son Co.*, 259 Fed. 830.

⁹ *Murphy v. Hanna*, 37 N. D. 156, L. R. A. 1918 B 135, 164 N. W. 33.

¹⁰ *Edwards v. International Pavement Co.*, 227 Mass. 206, 116 N. E. 266.

¹¹ *United Breweries Co. v. Price*, 197 Ill. App. 232.

¹² *Howard v. Tatum*, 81 W. Va. 56, 94 S. E. 965.

poration Act of Illinois cannot engage in the business of banking or lending money.¹³ A statutory provision forbidding loans by corporations to stockholders or officers is violated by giving a stockholder a note of the corporation for shares of its stock sold to a third person.¹⁴ A corporation's debt to a bank exceeded the amount permitted by the banking laws. The president of the debtor formed another company with dummy directors and executed a note to cover the excess indebtedness. It was held that the note was beyond the power of the company, the bank having knowledge of the scheme.¹⁵

¹³ American Credit & Trust Co. v. New Era Chandelier Co., 208 Ill. App. 181.

¹⁵ Taylor Feed Pen Co. v. Taylor Nat. Bank, — Tex. —, 215 S. W. 850.

¹⁴ In re Stucky Trucking & Rigging Co., 243 Fed. 287.

CHAPTER 26

POWERS AS TO NEGOTIABLE INSTRUMENTS

§ 951. General rule as to implied power to execute—Rule in United States.

§ 952. — Rule applied to particular corporations.

§ 955. Indorsement or other mode of transfer.

§ 956. Consideration, contents and requisites.

§ 957. Accommodation paper—Power to execute.

§ 959. — What is accommodation paper.

§ 960. — Liability of corporation.

§ 961. Defenses in actions on corporate paper.

§ 951. General rule as to implied power to execute—Rule in United States. Power to incur debts includes power to execute negotiable paper therefor.¹

§ 952. — Rule applied to particular corporations. An insurance company has power to issue negotiable paper,² and a railroad company may give its notes for money lawfully borrowed.³

§ 955. Indorsement or other mode of transfer. The consequences of an assignment of commercial paper by a corporation are no different than they would be in the case of a natural person.⁴ A corporation is liable as an indorsee of a note where it indorses it for purposes of its own and for a benefit accruing to it.⁵ A stockholder or officer of a corporation who indorses its negotiable notes should be held as indorser, so as not to be liable thereon in the absence of notice of dishonor.⁶

¹ *Western Nat. Bank v. Wittman*, 31 Cal. App. 615, 161 Pac. 137; *Webb & Co. v. Watkins*, 20 Ga. App. 436, 93 S. E. 108; *American Trust & Savings Bank v. A. Bauer Distilling & Importing Co.*, 205 Ill. App. 255; *Brown v. Boston & M. Ry.*, 233 Mass. 428, 124 N. E. 322; *Galveston-Houston Interurban Land Co. v. Dow*, — Tex. Civ. App. —, 193 S. W. 353.

² *Wells v. Manufacturers &*

Merchants Life Ass'n, 213 Ill. App. 549.

³ *Brown v. Boston & M. R. R.*, 233 Mass. 428, 124 N. E. 322.

⁴ *Central Bank v. Martin*, — Ind. App. —, 121 N. E. 57.

⁵ *East Coast Lumber & Supply Co. v. Maxwell*, — Fla. —, 80 So. 741.

⁶ *Tucker v. Mueller*, 287 Ill. 551, 122 N. E. 847.

It is no defense to a note in the hands of a bona fide holder, under the Negotiable Instruments Law, that the corporation payee had not filed its charter in the state where the note was executed and made payable.⁷

§ 956. Consideration, contents and requisites.⁸ A corporation may execute its note for the personal debt of its sole stockholder at least where there are no creditors.⁹ Want of the corporate seal on a note is no defense to the corporation maker which admits it received the money for which the note was given.¹⁰

§ 957. Accommodation paper—Power to execute. A corporation cannot execute or indorse negotiable paper for the accommodation of another.¹¹ A corporation cannot execute a note to a stockholder for the price of shares of stock sold by him to a third person.¹² A note of a corporation given in payment of the debt of an officer is not void but merely voidable at the instance of the corporation.¹³ Statutes often prohibit accommodation indorsements by banks.¹⁴

§ 959. — What is accommodation paper. An indorsement is not an accommodation one where the corporation received value and the indorsement was to accomplish its own legitimate ends.¹⁵

§ 960. — Liability of corporation. As between the immediate parties to a note given by a corporation, it is a defense that the note was merely accommodation paper.¹⁶

⁷ Despres, Bridges & Noel v. Hough Drug Co., — Miss. —, 86 So. 359.

⁸ Sufficiency of consideration, see Commercial Security Co. v. Modesto Drug Co., — Cal. App. —, 184 Pac. 964.

⁹ Sargent v. Palace Café Co., 175 Cal. 737, 167 Pac. 146.

¹⁰ Union Trust Co. v. Ensign-Baker Refining Co., 29 Cal. App. 641, 157 Pac. 613.

¹¹ In re Prospect Leasing Co., 250 Fed. 707; Newton v. Houston

Hot Well Improvement Co., — Tex. Civ. App. —, 211 S. W. 960.

¹² In re Stucky Trucking & Rigging Co., 243 Fed. 287.

¹³ Norment v. First Nat. Bank, 23 N. M. 198, 167 Pac. 731.

¹⁴ Sponge Exch. Bank v. Commercial Credit Co., 263 Fed. 20, Florida statute.

¹⁵ In re Prospect Leasing Co., 250 Fed. 707.

¹⁶ Phillips v. Interstate Land Co., 174 N. C. 542, 94 S. E. 12.

§ 961. Defenses in actions on corporate paper. A corporate note is valid although the proceeds were misappropriated.¹⁷ Where notes procured by fraud are transferred by a corporation to its president, he is not a bona fide holder in due course.¹⁸ A corporation cannot defeat liability on its note by attacking the validity of the stockholders' meeting authorizing the payment represented by the note.¹⁹

¹⁷ *Mitchell Street State Bank v. Froedtert*, — Wis. —, 170 N. W. 822.

¹⁸ *Duncan v. Carson*, — Va. —, 103 S. E. 665.

¹⁹ *Mitchell v. Forest City Printing Co.*, 187 N. Y. App. Div. 743, 176 N. Y. Supp. 157.

CHAPTER 27

POWERS AS TO BONDS, DEBENTURES AND COUPONS

I. DEFINITIONS AND NATURE AND KINDS OF

- § 962. Introductory.
- § 969. Kinds of bonds—Income bonds.

II. POWER TO ISSUE

- § 971. General rules.
- § 974. As dependent on purpose for which issued—Perpetual bonds.
- § 977. Conditions precedent—Consent of public service commission.
- § 979. Amount.

III. CONSIDERATION

- § 981. In general.
- § 982. Constitutional and statutory provisions.
- § 983. Paying or securing antecedent debts—In general.
- § 984. — Statutes as affecting power to pledge bonds.
- § 985. Issuance below par—General rule.
- § 988. — Pledge of bonds.
- § 990. — Statutes expressly forbidding or limiting to certain per cent.
- § 991. Bonds or stock as bonus.

IV. FORM AND CONTENTS

- § 992. General rules.
- § 994. Indorsement and certification.

V. SUBSCRIPTIONS, ISSUANCE, TRANSFERS AND OWNERSHIP

- § 996. Subscriptions—In general.
- § 999. — Rescission.
- § 1000. When bonds deemed “issued.”
- § 1002. Delivery.
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VI. EXCHANGE FOR STOCK OR NEW BONDS

- § 1008. Substitution of new bonds.

VII. NEGOTIABILITY

- § 1009. General rule.
- § 1011. As affected by contents of bond—General considerations.
- § 1012. — Applicability of Negotiable Instruments Law or other statutes.

VIII. WHO ARE BONA FIDE HOLDERS

- § 1015. Importance of question.
- § 1016. What law governs.
- § 1022. Notice—Actual notice.
- § 1023. — Constructive notice.
- § 1028. Presumptions and burden of proof.

IX. GUARANTY OF BONDS

- § 1029. Power to give.

X. PLEDGE OF BONDS

- § 1032. Power to pledge.
- § 1033. Rights of pledgee or purchaser from pledgee.

XI. DEFENSES

- § 1037. Want, inadequacy, failure or illegality of consideration.
- § 1042. Estoppel to set up defenses.

XII. MATURITY, SATISFACTION AND CANCELLATION

- § 1043. General rules.
- § 1045. Necessity for demand.
- § 1047. Sinking funds.
- § 1048. Collateral security.
- § 1049. Cancellation.

XIII. COUPONS

- § 1051. Negotiability.
- § 1053. Transfer.
- § 1060. Actions on coupons—Time to sue.

XIV. RIGHTS AND REMEDIES OF BONDHOLDERS

- § 1061. In general.
- § 1062. Right to sue on bonds or coupons—General rule.
- § 1064. Suit to set aside ultra vires act.
- § 1067. Rights of minority bondholders.
- § 1070. Stolen bonds.

I. DEFINITIONS AND NATURE AND KINDS OF

§ 962. Introductory. In determining whether a security is a bond or preferred stock, its substance rather than its form or name must be considered.¹

§ 969. Kinds of bonds—Income bonds.²

¹ In *re Collier's Estate*, — N. see *Edwards v. International Y. Misc.* —, 182 N. Y. Supp. 93, *Pavement Co.*, 227 Mass. 206, 116 and see § 3621, *infra*. N. E. 266.

² Construction of provisions in,

II. POWER TO ISSUE

§ 971. General rules. A private corporation has the power, unless forbidden, to issue negotiable bonds.³ However, a building and loan association has no power to issue negotiable bonds, etc., like other corporations.⁴

§ 974. As dependent on purpose for which issued—Perpetual bonds. But it is held in New York that a bond providing for a perpetual loan, while rare in this country, is not invalid merely because of the lack of maturity.⁵

§ 977. Conditions precedent—Consent of public service commission.⁶ Bond issues are sometimes prohibited except with consent of the public service commission and payment of certain fees to such commission for their approval.⁷ In Ohio, a railroad company cannot issue mortgage bonds without first applying to the public utilities commission.⁸ The Missouri statute requiring consent of the public service commission to an issuance of bonds by railroads does not apply to foreign corporations.⁹ A refusal by the public service commission of consent to the issuance of bonds cannot be sustained where unreasonable.¹⁰

The public utilities commission cannot, as a condition of granting an interstate railroad company permission to issue bonds, require it to pay one-tenth of one per cent of the amount of the total issue of bonds secured by mortgage on its entire system, which is practically all outside the state.¹¹

³ *Pratt v. Higginson*, 230 Mass. 256, 1 A. L. R. 714, 119 N. E. 661.

⁴ *In re German Savings & Loan Ass'n*, 253 Fed. 722.

⁵ *Schachne v. Corporation of Chamber of Commerce*, 102 N. Y. Misc. 197, 168 N. Y. Supp. 791, distinguishing *Taylor v. Philadelphia & R. R. Co.*, 7 Fed. 386.

⁶ *Powers of Public Utilities Commission of Kansas on application of interurban company to issue bonds*, see *Kansas City, K. V. & W. R. Co. v. Bristow*, 101 Kan. 557, L. R. A. 1918 E 342, 167 Pac. 1138.

⁷ See *Kansas City R. Co. v. Public Service Commission*, 273 Mo. 173, 201 S. W. 74.

⁸ See *Pollitz v. Public Utilities Commission*, 97 Ohio St. 191, 119 N. E. 507.

⁹ *Public Service Commission v. Union Pac. R. Co.*, 271 Mo. 258, 197 S. W. 39.

¹⁰ *Public Service Commission v. Union Pac. R. Co.*, 271 Mo. 258, 197 S. W. 39.

¹¹ *Missouri Pac. R. Co. v. Public Utilities Commission*, 292 Ill. 427, 127 N. E. 41.

§ 979. Amount.¹² Where a statute forbids increase of bonded indebtedness in excess of authorized capital, additional bonds cannot be issued where the bonds already equal the original capital and an attempted increase of stock was invalid.¹³

III. CONSIDERATION

§ 981. In general. Bonds must be based on a consideration.¹⁴ Where part of corporate bonds are valid and supported by a good consideration, their validity is not affected by the invalidity of other bonds given for the purchase of the corporation's own stock.¹⁵ Where bonds are delivered and part of the consideration for the transfer is acts to be performed in the future by the person to whom delivered, the failure to perform such acts is a total failure of consideration although part of the consideration for the transfer was past indebtedness.¹⁶

§ 982. Constitutional and statutory provisions. Bonds must be issued, under statutes in most states, either for money or property actually received, and if for the latter the purchase must be bona fide.¹⁷ Where a corporation increases its indebtedness, a part of which is for a full and valuable consideration and is a real increase, and a part of which is without consideration and is a fictitious increase, and the real increase is readily severable from the fictitious increase, the former is valid although the latter may be void or voidable.¹⁸

§ 983. Paying or securing antecedent debts—In general. Constitutional provisions or statutes often prohibit the issuance of bonds by corporations in payment of an antecedent debt.¹⁹

§ 984. — Statutes as affecting power to pledge bonds. Affirming the decisions in the Kemmerer and Mudge cases, Judge

¹² See also §§ 918, 920, *supra*.

¹³ *Hess Warming & Ventilating Co. v. Burlington Grain Elevator Co.*, — Mo. —, 217 S. W. 493.

¹⁴ See *Pueblo Foundry & Machine Co. v. Lannon*, — Colo. —, 187 Pac. 1031.

¹⁵ *Edgar v. Ames*, 255 Fed. 835.

¹⁶ *Mancourt-Winters Coal Co. v. St. Clair Paper Co.*, 260 Fed. 330.

¹⁷ *Big Spring Elec. Co. v. Kitzmiller*, — Pa. —, 110 Atl. 783.

¹⁸ *Edgar v. Ames*, 255 Fed. 835, 840, construing Oklahoma Constitution.

¹⁹ *Hess Warming & Ventilating Co. v. Burlington Grain Elevator Co.*, — Mo. —, 217 S. W. 493.

Sanborn states the rule as settled that corporate bonds issued "to secure an antecedent debt with no new consideration except an extension of the time of payment, are void" as violating a constitutional provision prohibiting corporations from issuing bonds except for labor done or money or property actually received.²⁰

§ 985. Issuance below par—General rule. A solvent corporation may dispose of its bonds at less than par, where no creditor is injured thereby.²¹

§ 988. — Pledge of bonds. At common law a corporation may pledge its bonds in excess of the debt where done in good faith.²² In New York a corporation has the power to pledge its bonds at less than par as collateral to a loan.²³

§ 990. — Statutes expressly forbidding or limiting to certain per cent. The Wisconsin statute is further considered by the Federal Circuit Court of Appeals by holding that there need be no stipulation taken from the pledgee or purchaser agreeing to account for the collateral bonds at not less than 75 per cent of their par value.²⁴

§ 991. Bonds or stock as bonus. Where stockholders all consent, bonds may be issued to stockholders, where no third persons are injured.²⁵ But in some jurisdictions, where bonds are issued to stockholders as a bonus, the holders have no standing as creditors, and the corporation is entitled to relief in equity to prevent such bonds getting into the hands of bona fide holders.²⁶

²⁰ Lyon v. Bleeg, 240 Fed. 405, South Dakota Constitution.

This rule is also adopted in Missouri in Hess Warming & Ventilating Co. v. Burlington Grain Elevator Co., — Mo. —, 217 S. W. 493.

²¹ Pueblo Foundry & Machine Co. v. Lannon, — Colo. —, 187 Pac. 1031.

²² United States Cast Iron Pipe & Foundry Co. v. Henry Vogt Mach. Co., 182 Ky. 473, 206 S. W. 806.

²³ Westinghouse Elec. & Mfg. Co. v. Brooklyn Rapid Transit Co., 256 Fed. 465.

²⁴ In re Valencia Condensed Milk Co., 240 Fed. 338, rev'g 233 Fed. 173.

²⁵ Pueblo Foundry & Machine Co. v. Lannon, — Colo. —, 187 Pac. 1031.

²⁶ Williamson v. Collins, 243 Fed. 835.

IV. FORM AND CONTENTS

§ 992. General rules. Bonds of a corporation may expressly preclude further mortgaging of the corporate property, except as provided therein, so as to create an equitable lien on unmortgaged property.²⁷

§ 994. Indorsement and certification. Bonds are invalid where by their terms they must be certified by the trustee who was authorized to certify only on certificate of the president and chief engineer, where certified only on the certificate of the engineer who had ceased to act as such several years before.²⁸ A certificate that each bond to which it is attached is one of a series of nineteen hundred bonds and that the coupons are "genuine," does not cover the legal sufficiency of the security. The purpose of such certification is merely to prevent an over-issue.²⁹

V. SUBSCRIPTIONS, ISSUANCE, TRANSFERS AND OWNERSHIP

§ 996. Subscriptions—In general. Fraud inducing subscriptions is of course material.³⁰ Pre-emptive right of stockholders to subscribe to new stock does not extend to bonds having an incidental stock conversion privilege.³¹

§ 999. — Rescission. If a purchase of bonds is induced by false representations of an agent of the corporation, the subscriber may rescind his subscription. But mere expressions of opinion as to value are not actionable misrepresentations and the right to rescind may be lost by acquiescence.³²

§ 1000. When bonds deemed "issued." Corporate bonds pledged to secure a corporate debt are issued, when pledged,

²⁷ Connecticut Co. v. New York, N. H. & H. R. Co., — Conn. —, 107 Atl. 646.

²⁸ Stewart v. Florida, G. & W. Ry. Co., 255 Fed. 616.

²⁹ Ainsa v. Mercantile Trust Co., 174 Cal. 504, 163 Pac. 898.

³⁰ Columbia Knickerbocker Trust Co. v. Abbot, 247 Fed. 833,

851, where mortgage was represented to be a first lien.

³¹ Venner v. American Telegraph & Telephone Co., 110 N. Y. Misc. 118, 181 N. Y. Supp. 45.

³² Brice v. Mt. Scott Park Cemetery Corporation, 91 Ore. 333, 178 Pac. 935.

without regard to who holds the legal title to them during their hypothecation.³³

§ 1002. Delivery. Where bonds are delivered as payment or as collateral but conditionally, then of course the person to whom delivered is not entitled to them or their value unless he fulfils the conditions.³⁴ Unexplained delay of over twenty years to secure delivery of bonds is such laches as bars relief.³⁵

§ 1004. Transfers.³⁶ Fraudulent representations as to value of corporate bonds exchanged for land are actionable.³⁷

VI. EXCHANGE FOR STOCK OR NEW BONDS

§ 1008. Substitution of new bonds. The right to demand the issuance of bonds in exchange for interim certificates may be waived by the acts of the creditor.³⁸

VII. NEGOTIABILITY

§ 1009. General rule. Corporate bonds are negotiable.³⁹ Innocent holders of bonds may, in Ohio, enforce the lien of the mortgage free from defenses which would be good as between the original parties.⁴⁰ Bonds non-negotiable in form do not in California, become negotiable after the first holder has sold them nor as against all persons other than the obligor.⁴¹

§ 1011. As affected by contents of bond—General considerations. A bond is not negotiable merely because payable to

³³ *Smith v. Pillsbury*, 39 Cal. App. 240, 178 Pac. 719.

³⁴ *Mancourt-Winters Coal Co. v. St. Clair Paper Co.*, 260 Fed. 330.

³⁵ *Stewart v. Florida, G. & W. Ry. Co.*, 255 Fed. 616.

³⁶ Rights of purchaser on breach of warranty of worthless corporate bond, see *Burtch v. Child, Huls-wit & Co.*, 207 Mich. 205, 174 N. W. 170.

Interest accruing on bonds as belonging to purchasers of bonds, see *Reynolds v. Pfister*, 166 Wis. 137, 164 N. W. 843.

³⁷ *Pearson v. Wallace*, 204 Mich. 643, 170 N. W. 72.

³⁸ See *Smith v. Central & Pacific Improvement Co.*, — Cal. App. —, 187 Pac. 456.

³⁹ *Pratt v. Higginson*, 230 Mass. 256, 1 A. L. R. 714, 119 N. E. 66.

Bonds of irrigation district are negotiable, see *Rialto Irrigation Dist. v. Stowell*, 246 Fed. 294.

⁴⁰ *Williamson v. Collins*, 24 Fed. 835, 840.

⁴¹ *Crocker Nat. Bank of San Francisco v. Byrne & McDonnell*, 178 Cal. 329, 173 Pac. 752.

bearer.⁴² The provision in a bond that the holder at maturity will receive the face of the bond in money, or at his option an equivalent in stock of the corporation, does not destroy negotiability.⁴³ A guaranty of payment indorsed on corporate bonds does not affect their negotiability.⁴⁴ In California, corporate bonds are not negotiable where they state on their face that they are secured by trust deeds or mortgages.⁴⁵ In New York, a reference in bonds to the mortgage or deed of trust of even date, for a description of the property mortgaged and the nature and extent of the rights of the holders of the bonds and the terms and conditions under which the bonds were issued, does not affect their negotiability.⁴⁶

Interim certificates, i.e., paper given to certify that the bearer, upon the surrender of the certificate is entitled to receive bonds when issued and delivered to a trust company, are not negotiable where not signed by the corporation which is to issue the bonds, do not contain an express promise to pay a sum certain in money, etc.⁴⁷

§ 1012. — Applicability of Negotiable Instruments Law or other statutes. Custom cannot affect negotiability where contrary to a positive statute.⁴⁸ Negotiability of corporate bonds is to be determined by the Negotiable Instruments Law and not by any custom.⁴⁹ Bonds are payable "at a fixed or determinable future time," within the Negotiable Instruments Law, although the holders may accelerate the date of maturity on failure to pay interest.⁵⁰

⁴² Crocker Nat. Bank of San Francisco v. Byrne & McDonnell, 178 Cal. 329, 173 Pac. 752.

⁴³ Pratt v. Higginson, 230 Mass. 256, 1 A. L. R. 714, 119 N. E. 661.

⁴⁴ Higgins v. Hocking Valley Ry. Co., 188 N. Y. App. Div. 684, 177 N. Y. Supp. 444.

⁴⁵ Crocker Nat. Bank of San Francisco v. Byrne & McDonnell, 178 Cal. 329, 173 Pac. 752; King v. Harford, — Cal. App. —, 191 Pac. 998.

⁴⁶ Higgins v. Hocking Valley R. Co., 188 N. Y. App. Div. 684, 177 N. Y. Supp. 444.

⁴⁷ Babcock v. National Surety Co., 106 N. Y. Misc. 149, 175 N. Y. Supp. 432.

⁴⁸ Crocker Nat. Bank of San Francisco v. Byrne & McDonnell, 178 Cal. 329, 173 Pac. 752.

⁴⁹ Higgins v. Hocking Valley R. Co., 188 N. Y. App. Div. 684, 177 N. Y. Supp. 444; Babcock v. National Surety Co., 106 N. Y. Misc. 149, 175 N. Y. Supp. 432. See also Parks v. Hughes, 145 La. 221, 82 So. 202.

⁵⁰ Higgins v. Hocking Valley R. Co., 188 N. Y. App. Div. 684, 177 N. Y. Supp. 444.

VIII. WHO ARE BONA FIDE HOLDERS

§ 1015. Importance of question.⁵¹

§ 1016. **What law governs.** Whether the holder is a bona fide holder for value of corporate bonds is, as between the corporation and the holder, to be determined by the law of the state where the corporation was created and the bonds issued rather than of the state where the transfer to the holder by another was made.⁵²

§ 1022. **Notice—Actual notice.** One who takes corporate bonds with notice of defects is not a bona fide holder.⁵³ Notice of an agent of the bondholders is notice to the bondholders themselves.⁵⁴

§ 1023. — **Constructive notice.** Knowledge of infirmities in corporate bonds is imputed to certain stockholders where they are uniformly represented by certain officers and others who had knowledge thereof.⁵⁵

§ 1028. Presumptions and burden of proof.⁵⁶

IX. GUARANTY OF BONDS

§ 1029. **Power to give.**⁵⁷ A railroad company has no incidental power to guarantee the bonds of another railway company, in ordinary cases.⁵⁸ But a corporation has power to

⁵¹ Who are holders in due course, see *Williamson v. Collins*, 243 Fed. 835, 843.

⁵² *Badger Machinery Co. v. Columbia County Elec. Light & Power Co.*, — Wis. —, 163 N. W. 188.

⁵³ *Hess Warming & Ventilating Co. v. Burlington Grain Elevator Co.*, — Mo. —, 217 S. W. 493.

⁵⁴ *Parks v. Hughes*, 145 La. 221, 82 So. 202.

⁵⁵ *Parks v. Hughes*, 145 La. 221, 82 So. 202.

⁵⁶ Shifting of burden of proof, see *Parks v. Hughes*, 145 La. 221, 82 So. 202.

⁵⁷ Guaranty of bonds, effect of judgment against guarantor, see *Hamer v. New York Rys. Co.*, 244 U. S. 266, 61 L. Ed. 1125.

Contract construed as guaranty of payment of interest on mortgage bonds of railroad company, see *Equitable Trust Co. v. Denver & R. G. R. Co.*, 250 Fed. 327.

For note on "Right of railroad company to guarantee the securities of another railroad company," see *L. R. A.* 1918 D 175.

⁵⁸ *Pollitz v. Michigan Railroad Commission*, 205 Mich. 549, 172 N. W. 611.

guarantee the bonds of a subsidiary, pursuant to power expressly conferred on the guarantor to render financial aid to the obligor; and where "one corporation is authorized to acquire the stock of another, and to aid it in carrying out its objects, a guaranty by the former of the latter's obligations is valid, where it carries forward some of the powers expressly granted to the guaranteeing company."⁵⁹ A corporation is not precluded from guaranteeing bonds of its subsidiary by the Constitution of Washington providing that corporations shall not issue any "bond or other obligation for the payment of money" except for money or property received or labor done.⁶⁰

A railroad company has power, in order to sell bonds of another company taken by it as security, to guarantee their payment.⁶¹ But a railroad company has no power to guarantee, jointly with others, an entire issue of bonds of another company of which it owns only a portion.⁶² The opinion of the state railroad commission authorizing a railroad company to guarantee bonds of another company does not validate such a guaranty as to the state or stockholders, where beyond the powers of the corporation.⁶³

A guaranty by a corporation of the "principal and interest on the bonds" of another company is a guaranty of payment and not merely of collection.⁶⁴

X. PLEDGE OF BONDS

§ 1032. Power to pledge. A corporation may pledge as security for its debts its own bonds which have never been issued.⁶⁵

§ 1033. Rights of pledgee or purchaser from pledgee. A pledgee of bonds may sell them on default.⁶⁶ The pledgee has

⁵⁹ *General Inv. Co. v. Bethlehem Steel Corporation*, 248 Fed. 303.

⁶⁰ *Lumbermen's Trust Co. v. Title Ins. & Inv. Co.*, 248 Fed. 212, 220.

⁶¹ *Pollitz v. Public Utilities Commission*, 96 Ohio St. 49, L. R. A. 1918 D 166, 117 N. E. 149. See also *Higgins v. Hocking Valley R. Co.*, 188 N. Y. App. Div. 684, 177 N. Y. Supp. 444.

⁶² *Pollitz v. Public Utilities Commission*, 96 Ohio St. 49, L. R. A. 1918 D 166, 117 N. E. 149.

⁶³ *Pollitz v. Michigan Railroad Commission*, 205 Mich. 549, 172 N. W. 611.

⁶⁴ *Graysonia-Nashville Lumber Co. v. Goldman*, 247 Fed. 423.

⁶⁵ *Worth v. Marshall Field & Co.*, 240 Fed. 395.

⁶⁶ *Miller v. American Bank &*

the right to collect the interest coupons when due and the principal of the bonds on their maturity.⁶⁷ But where bonds are deposited as collateral, and the interest on the debt is kept paid, the pledgee is not entitled to the interest accruing on the bonds.⁶⁸ A pledge of bonds having no coupons but with interest payable in semiannual instalments does not transfer the right to interest due but not paid before the transfer.⁶⁹

Where a corporation pledges its bonds, the pledgees were held "bondholders" entitled to vote as such.⁷⁰

Where one puts up bonds with a stockbroker and he wrongfully pledges them, the bona fide pledgees may sell them to satisfy the debt for which pledged, but not until other security pledged is realized on.⁷¹

A pledgee of bonds may recover from the holder of the majority of the bonds for loss resulting from the latter's breach of agreement to give notice to the pledgee of any sale, where the sale was a private one under the direction of the majority holder and without notice to the pledgee.⁷²

XI. DEFENSES

§ 1037. Want, inadequacy, failure or illegality of consideration. Where bonds are delivered either as payment or as collateral security for an open account for coal, on a promise to increase the amount of coal shipped, the failure to so increase the shipments of coal constitutes a failure of consideration so that the creditor is not entitled to the bonds, although part of the consideration was past indebtedness.⁷³

§ 1042. Estoppel to set up defenses. Stockholders who participate in a bond issue are estopped to deny its legality.⁷⁴

Trust Co., — W. Va. —, 100 S. E. 864.

⁶⁷ Smith v. Pillsbury, 39 Cal. App. 240, 178 Pac. 719.

⁶⁸ Worth v. Marshall Field & Co., 240 Fed. 395.

⁶⁹ Federal Cement Co. v. Shaffer, 238 Fed. 245.

⁷⁰ Heath v. Port of Para, 262 Fed. 815.

⁷¹ Gouert v. Mechanics' & M. Nat. Bank, 191 N. Y. App. Div. 854, 182 N. Y. Supp. 579.

⁷² First Nat. Bank v. Franklin Bank, — Mo. —, 211 S. W. 3.

⁷³ Mancourt-Winters Coal Co. v. St. Clair Paper Co., 260 Fed. 330.

⁷⁴ Pueblo Foundry & Machine Co. v. Lannon, — Colo. —, 187 Pac. 1031.

XII. MATURITY, SATISFACTION AND CANCELLATION

§ 1043. General rules. A bond issued by a Chamber of Commerce to subscribers to a building fund providing that it shall be redeemable at any time at the option of the corporation but not otherwise fixing any time for payment, is not payable in a reasonable time but instead is a perpetual loan.⁷⁵

§ 1045. Necessity for demand. When no particular place of payment is fixed, the corporation must seek debenture holders, if within the realm, and tender payment on the date the debentures are due.⁷⁶

§ 1047. Sinking funds.⁷⁷ Mortgage provisions as to a sinking fund apply to bonds delivered to the trustee as custodian but pledged by the corporation on various occasions.⁷⁸

§ 1048. Collateral security.⁷⁹

§ 1049. Cancellation.⁸⁰

XIII. COUPONS

§ 1051. Negotiability. One taking a coupon after the date of its maturity takes it subject to all equities then outstanding against it, although as to the bond itself and as to other coupons

⁷⁵ *Schachne v. Corporation of Chamber of Commerce*, 102 N. Y. Misc. 197, 168 N. Y. Supp. 791.

⁷⁶ *Fowler v. Midland Electric Corporation for Power Distribution, Ltd.*, [1917] 1 Ch. Div. 656.

⁷⁷ Right to withdraw securities from sinking fund, see *Hudson Nav. Co. v. Union Trust Co. of Albany*, 186 N. Y. App. Div. 850, 174 N. Y. Supp. 852.

Rights in sinking fund and suits to recover, see *Brown v. Pennsylvania Canal Co.*, 244 Fed. 980.

⁷⁸ *Bankers' Trust Co. v. Denver Tramway Co.*, — N. Y. App. Div. —, 183 N. Y. Supp. 326.

⁷⁹ Construction and effect of agreement whereby corporation issuing bonds which had deposited with a trustee securities with the right on surrender of any bond to select and withdraw a proportional amount of the security, where thereafter receivers were appointed for the corporation, see *Robinson v. Security Trust Co.*, — Conn. —, 108 Atl. 665.

⁸⁰ Bonds as canceled by depositing them with trustee under agreement for a new mortgage, see *Belleville Sav. Bank v. Mercantile Trust Co.*, 194 Ill. App. 175.

maturing at subsequent dates, he may be a purchaser for value without notice.⁸¹

§ 1053. Transfer.⁸²

§ 1060. Actions on coupons—Time to sue. Actions on coupons are governed by the same limitations applicable to the bonds except that limitations begin to run from the maturity of the coupon and not of the bond.⁸³

XIV. RIGHTS AND REMEDIES OF BONDHOLDERS

§ 1061. In general. Bondholders are entitled to relief in equity by canceling certificates of indebtedness, in a proper case.⁸⁴ Bondholders may, it seems, enforce specific performance of a contract between the corporation and a third person, where its abandonment would leave the bondholders without security.⁸⁵ Bondholders of an irrigation company may enforce in equity the obligation of the company to devote the proceeds to irrigation purposes.⁸⁶ Where a mortgage secured two issues of bonds, a contract by a third person to contribute to payment of the first series of bonds which were a prior lien, is enforceable by holders of the second series as one for their direct benefit.⁸⁷ Bondholders who claim no fraud nor improper or tortious acts of corporate officers have no cause of action against another corporation to charge it and its property with liability on the bonds, merely because the same persons control both corporations and defendant has caused the mortgagor to lease and operate other properties to its own detriment but to the benefit of the other company.⁸⁸

⁸¹ *Worth v. Marshall Field & Co.*, 240 Fed. 395.

⁸² Interest coupons as belonging to buyer or seller of bonds, as dependent on time when title passed, see *Gamble v. Hollenbach*, 188 Ky. 685, 223 S. W. 833.

⁸³ *Smythe v. Inhabitants of New Providence Tp.*, 253 Fed. 824.

⁸⁴ *McGaw v. Hoen*, 133 Md. 672, 106 Atl. 13.

⁸⁵ *Gas Securities Co. v. Antero & Lost Park Reservoir Co.*, 259 Fed. 423.

⁸⁶ *Gas Securities Co. v. Antero & Lost Park Reservoir Co.*, 259 Fed. 423.

⁸⁷ *Wheeling & L. E. R. Co. v. Carpenter*, 264 Fed. 772.

⁸⁸ *Allen v. Philadelphia Co.*, 265 Fed. 807, *aff'd* 265 Fed. 817.

A bondholder secured by mortgage cannot sue to impose a lien for the benefit of all the bondholders on property not subject to the mortgage, and to prevent the dismemberment of a street railway system of which the mortgaged premises constituted a part, where there is nothing to show that the mortgage trustee has been requested, and has refused, to bring the suit.⁸⁹

§ 1062. Right to sue on bonds or coupons—General rule. Where the bonds of a New York corporation executed in New York were secured by a mortgage on property in New Jersey conveyed under a trust agreement to a New York trust company, the owner of bonds may sue in New York to recover thereon without first foreclosing the mortgage as required by the New Jersey statute. In such a case the law of New York applies.⁹⁰

§ 1064. Suit to set aside ultra vires act. But bondholders may sue in equity to cancel certificates of indebtedness where unlawfully issued by the corporation.⁹¹

§ 1067. Rights of minority bondholders. Majority bondholders cannot obtain a preference over minority bondholders, after the corporation has ceased to do business, by virtue of a provision in the mortgage giving the owners of two-thirds of the bonds the power to modify the mortgage, etc.⁹²

§ 1070. Stolen bonds. If received by a holder in due course, the owner loses his rights to stolen bonds.⁹³ But if bonds are non-negotiable, the title of one who takes them from a thief will not prevail as against the true owner.⁹⁴ The bona fide holder of non-negotiable stolen interim certificates to be exchanged for bonds obtains no title to them.⁹⁵

⁸⁹ Allen v. Philadelphia Co., 265 Fed. 807, 815.

⁹⁰ Thompson v. Lakewood City Development Co., 105 N. Y. Misc. 580, 174 N. Y. Supp. 825.

⁹¹ McGaw v. Hoen, 133 Md. 672, 106 Atl. 13.

⁹² Vogelstein v. Athletic Min. Co., — Mo. App. —, 192 S. W. 760.

⁹³ Pratt v. Higginson, 230 Mass. 256, 1 A. L. R. 714, 119 N. E. 661.

⁹⁴ Crocker Nat. Bank of San Francisco v. Byrne & McDonnell, 178 Cal. 329, 173 Pac. 752.

⁹⁵ Babcock v. National Surety Co., 106 N. Y. Misc. 149, 175 N. Y. Supp. 432.

CHAPTER 28

ACQUISITION AND HOLDING OF PERSONAL PROPERTY

§ 1072. General rules.

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§ 1074. — For use outside of authorized business.

§ 1075. — Taking in payment of debt or as security.

§ 1076. Power to take and hold choses in action—**In general.**

§ 1079. Constitutional or statutory restrictions.

§ 1080. Ownership.

§ 1072. General rules. Corporations may take a bequest by will unless otherwise provided by statute.¹ In determining which of two corporations was intended to be the legatee of a bequest to the "Old Ladies Home," the court may examine their charters to determine their powers.² A corporation having control of a church may take a legacy on behalf of an unincorporated church having no power to take as legatee.³ A bequest to a branch of an incorporated society, where the branch is unincorporated and therefore cannot take, goes to the society itself.⁴ A contract of sale of merchandise to a corporation under which payment was to be made from the proceeds of sales of shares of stock is not breached by the buyer where it turns over all such proceeds.⁵

§ 1073. Purposes for which property may be acquired—In general. A packing company has power to purchase crude glycerine.⁶ A corporation created to conduct a general automo-

¹In *re Dol's Estate*, — Cal. —, 187 Pac. 428.

Power of college to accept gift to erect memorial chapel, see *Lightfoot v. Poindexter*, — Tex. Civ. App. —, 199 S. W. 1152.

²In *re Seabury's Estate*, 107 N. Y. Misc. 705, 177 N. Y. Supp. 91.

³*Kernoehan v. Farmers' Loan &*

Trust Co., 187 N. Y. App. Div. 668, 175 N. Y. Supp. 831.

⁴In *re Cameron's Estate*, 113 N. Y. Misc. 416, 184 N. Y. Supp. 540.

⁵In *re Blue Earth County Co-Op. Co.*, 139 Minn. 231, 166 N. W. 178.

⁶*Illinois Cudahy Packing Co. v*

bile and taxicab business has power to buy automobile supplies without regard to how they are used.⁷ A lumber company having the right to engage in the manufacture of salt as an incidental business, using waste wood and coal to evaporate the brine, has power to replace worn-out salt apparatus with a new system permitting greater salt production with less fuel.⁸ A cotton gin company has power to buy cotton seed from customers, according to custom, to retain their business.⁹

A corporation chartered for general educational purposes has power to accept and use a legacy left to it to construct a church on its own property.¹⁰ An educational corporation such as a college may accept a bequest of money for erection of a chapel to be used for religious services.¹¹

§ 1074. — For use outside of authorized business.¹²

§ 1075. — Taking in payment of debt or as security. A national bank may purchase cars of grain as an incident to the purchase of a draft with bill of lading attached.¹³

§ 1076. Power to take and hold choses in action—In general.¹⁴ A corporation which owns stock in another corporation has power to purchase bonds of the latter to safeguard and further its interests as a stockholder.¹⁵

Kansas City Soap Co., 247 Fed. 556.

⁷ Shapleigh Hardware Co. v. Lewis, 118 Miss. 586, 79 So. 765.

⁸ Ruggles v. Buckley & Douglas Lumber Co., 210 Mich. 58, 177 N. W. 270.

⁹ Bishop Mfg. Co. v. Sealy Oil Mill & Manufacturing Co., — Tex. Civ. App. —, 220 S. W. 203.

¹⁰ President & Council of Mt. St. Mary's College v. Williams, 132 Md. 184, 103 Atl. 479.

¹¹ Lightfoot v. Poindexter, — Tex. Civ. App. —, 199 S. W. 1152.

A gift to a college of money to be used to erect a memorial chapel for religious services is not

void on the theory that an educational corporation cannot own a building to be used for conducting religious services. Lightfoot v. Poindexter, — Tex. Civ. App. —, 199 S. W. 1152.

¹² See generally §§ 847, 1073, supra.

¹³ Citizens' Bank & Trust Co. v. Harpeth Nat. Bank, 120 Miss. 505, 82 So. 329.

¹⁴ Statute authorizes purchase of bonds in Pennsylvania. Wrightsville Hardware Co. v. McElroy, 254 Pa. 422, 98 Atl. 1052.

¹⁵ Pollitz v. Public Utilities Commission, 96 Ohio St. 49, L. R. A. 1918 D 166, 117 N. E. 149.

§ 1079. Constitutional or statutory restrictions. A state bank is not limited as to the amount of United States bonds it may purchase or hold by a statute providing that total liabilities of "any person, corporation or copartnership" to such a bank shall not exceed fifteen per cent of its capital and surplus.¹⁶ In some states, statutes forbid bequests or devises to a charitable or benevolent society in trust for charitable uses unless the will was executed at least thirty days before the death of the testator.¹⁷

The constitutional provision that "neither the credit nor the money of the state shall be given or loaned to or in aid of any * * * corporation" does not prevent the recognition of corporate claims against the state, where based on equity and justice.¹⁸

A municipality has no power to issue municipal bonds to replace, renew or repair the tracks of a street railway company, where the state constitution forbids raising money to aid any joint stock corporation.¹⁹

§ 1080. Ownership.²⁰ A gift to trustees of a corporation is a gift to the corporation.²¹ A direct gift to a charitable corporation is not a trust in the eye of the law but is a charitable donation.²² A railway company cannot refuse to restore railway material to its admitted owner on the theory that the property has been dedicated to a public use.²³

¹⁶ *Trumer v. South Side State Bank*, 139 Minn. 222, 166 N. W. 127.

¹⁷ *In re Dol's Estate*, — Cal. —, 187 Pac. 428.

¹⁸ *Oswego & S. R. Co. v. State*, 226 N. Y. 351, 124 N. E. 8, aff'g 186 N. Y. App. Div. 384, 173 N. Y. Supp. 609.

¹⁹ *City of Cincinnati v. Harth*, — Ohio St. —, 128 N. E. 263.

²⁰ See also § 1072, *supra*.

²¹ *In re Allen's Will*, 111 N. Y. Misc. 93, 181 N. Y. Supp. 398.

²² *In re Allen's Will*, 111 N. Y. Misc. 93, 181 N. Y. Supp. 398.

²³ *Ocmulgee River Lumber Co. v. Ocmulgee Valley R. Co.*, 251 Fed. 161.

CHAPTER 29

ACQUISITION AND HOLDING OF REAL PROPERTY

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§ 1082. Power as incidental. Every corporation has the implied power to acquire and own real estate unless there is some

special law or a provision in the charter to the contrary.¹ A declaration in the charter of a charitable corporation that it has neither capital stock nor assets does not preclude power of the corporation to accept a donation of real property.²

II. POWER AS DEPENDENT ON PURPOSE FOR WHICH ACQUIRED OR USED

§ 1086. General rules. A purchase of land is not within corporate powers merely because it is a profitable investment.³

§ 1087. Amount in excess of actual necessity. Land not necessary to the conduct of the business cannot be acquired.⁴

§ 1089. Purchase for speculation.⁵

§ 1095. Application of rules to particular corporations—Railroad companies. Railroad land held in anticipation of future use for legitimate and necessary purposes cannot be forfeited by the state, under the Kentucky statutes.⁶

III. STATUTES OR CONSTITUTIONAL PROVISIONS AS GRANTING OR LIMITING POWER

§ 1097. Grant of power—General considerations. A grant by the state to a corporation of power to acquire and enjoy real estate without limit as to value and quantity is a contract which cannot be impaired by a subsequent statute where no right to repeal or amend the charter has been reserved.⁷

¹Sisters of Charity of Incarnate Word v. Emery, 144 La. 614, 81 So. 99.

In Texas an irrigation company may acquire land. Westbrook v. Missouri-Texas Land & Irrigation Co., — Tex. Civ. App. —, 195 S. W. 1154.

But in North Carolina it seems to be held that a railroad company has no power to acquire or hold except by statutory authority. Wallace v. Moore, 178 N. C. 114, 100 S. E. 237.

²Sisters of Charity of Incarnate

Word v. Emery, 144 La. 614, 81 So. 99.

³National Equitable Society v. Alexander, — Tex. Civ. App. —, 220 S. W. 184.

⁴Hallam v. Bailey, — Okla. —, 166 Pac. 874.

⁵That a college may purchase property for purpose of development and sale, see Diggs v. Morgan College, 133 Md. 264, 105 Atl. 157.

⁶Chesapeake & O. R. Co. v. Com., 189 Ky. 465, 225 S. W. 145.

⁷Southern Realty Co. v. Tchula

§ 1099. **Express or implied prohibition—In general.** A constitutional provision prohibiting corporations from acquiring real estate, except such as is necessary, is not self-executing, and real estate acquired in violation thereof does not ipso facto escheat to the state.⁸

§ 1102. — **Restriction as to quantity or value.** In Oklahoma the 1908 statute requiring corporations to dispose of real property not used in the business, except real estate in cities or towns owned at the time the act became effective, within seven years, was not repealed by the Act of May 27, 1908.⁹

§ 1103. — **Restriction to amount reasonably necessary.** If land is being held by a corporation in anticipation of future use for corporate purposes, and is accompanied by an ever-present intention to devote it to such use, the Kentucky constitutional provision and statute forbidding corporations to own real estate not necessary for carrying on its business for longer than five years does not apply; and the intention to so devote the property to corporate use need not be shown by any acts at a formal meeting of the board of directors.¹⁰ The Kentucky prohibition against corporations holding real property not necessary for business purposes for more than five years does not apply where the corporation in good faith acquires it for a necessary purpose and holds the property with the bona fide intent to devote it to a necessary purpose;¹¹ and such a statute does not impair the obligation of a contract where the charter does not confer the right to hold unnecessary land.¹²

A state has the right to escheat land held by a national bank, in violation of a state statute fixing five years as the limit for holding real estate not necessary for use, the National Banking Act containing the same prohibition.¹³

Co-Operative Stores, 114 Miss. 309, 75 So. 121.

⁸ Parival Inv. Co. v. State, — Okla. —, 175 Pac. 514.

⁹ State v. Prairie Oil & Gas Co., — Okla. —, 167 Pac. 756.

¹⁰ Com. v. Mehler & Eckstempker Lumber Co., 183 Ky. 11, 208 S. W. 13.

¹¹ Com. v. Clark County Nat. Bank, 187 Ky. 151, 219 S. W. 175.

Forfeiture can be enforced only by the state. Chesapeake & O. R. Co. v. Rosskamp, 179 Ky. 175, 200 S. W. 496.

¹² Com. v. Clark County Nat. Bank, 187 Ky. 151, 219 S. W. 175, following Germania Ins. Co. v. Com., 141 Ky. 606, 133 S. W. 393.

¹³ Com. v. Clark County Nat. Bank, 187 Ky. 151, 219 S. W. 175.

A purchase of real estate to compromise a demand against the corporation for breach of contract is beyond corporate power where a statute prohibits purchases of real estate by corporations except so far as necessary to enable them to do business.¹⁴

§ 1105. — Exception of particular purposes. In Mississippi a statute prohibits the ownership of land by a corporation for agricultural purposes. This statute is not violated by the acquisition of farming land but only by the acquisition of it for agricultural purposes.¹⁵

IV. MODE OF ACQUISITION

§ 1107. General rules. A corporation may acquire title to land by adverse possession.¹⁶ Power to acquire title by purchase implies the right to acquire title by donation.¹⁷ A corporation created to care for the sick in hospitals, to care for insane persons, incurables, aged people and foundlings, and to conduct orphan asylums and a training school for nurses, has power to receive a donation of realty.¹⁸

§ 1108. Power to take by devise.¹⁹ In the absence of legislation to the contrary, a testator may legally devise lands in one state to a corporation created under the laws of another state.²⁰ A devise to a corporation may be conditional.²¹ A devise to a

¹⁴ *National Equitable Society v. Alexander*, — Tex. Civ. App. —, 220 S. W. 184.

¹⁵ *Middleton v. Georgetown Mercantile Co.*, 117 Miss. 134, 77 So. 956.

This statute does not apply, however, as to corporations created before its passage whose charter gave them the right without limit to own and hold land. *Southern Realty Co. v. Tchula Co-Operative Stores*, — Miss. —, 75 So. 121.

¹⁶ *Cross v. Seaboard Air Line Ry. Co.*, 172 N. C. 119, 90 S. E. 14.

¹⁷ *Sisters of Charity of Incar-*

nate Word v. Emery, 144 La. 614, 81 So. 99.

¹⁸ *Sisters of Charity of Incarnate Word v. Emery*, 144 La. 614, 81 So. 99.

¹⁹ Religious corporation, by statute, may acquire property by devise. *Potter v. Pike*, — N. Y. App. Div. —, 183 N. Y. Supp. 842.

Power to take personal property by bequest, see § 1072, *supra*.

²⁰ *Sisters of Charity of Incarnate Word v. Emery*, 144 La. 614, 81 So. 99.

²¹ *Sisters of Charity of Incarnate Word v. Emery*, 144 La. 614, 81 So. 99.

charitable corporation is not void because it and its successors may cease to exist.²²

Under a statute providing that no corporation can take under a will "unless expressly authorized by charter or by statute," it is sufficient that the authority be conferred by the articles of incorporation where a company is created under a general law, since the word "charter" as used therein includes articles of incorporation.²³

The proportion of one's estate a person may devise or bequeath to a charitable corporation is sometimes limited by statute, where the testator has a husband, wife, child or parent.²⁴

V. TITLE ACQUIRED AND LIABILITIES ASSUMED

§ 1110. General rules. A grant of a railroad right of way to a corporation, or to perpetual trustees holding for corporate uses, does not need words of succession in order to be perpetual.²⁵

§ 1111. Power to take fee simple. Corporations may take title in fee to real property. The statutes of mortmain have never been adopted in North Carolina.²⁶ A railway company may acquire the fee in real property.²⁷

§ 1112. Title as limited to life of corporation. The fact that the charter of a corporation limits the term of the charter to fifty years does not preclude the power to take title to realty in perpetuity.²⁸ A charitable corporation may accept a donation in perpetuity although the term of its charter is limited to fifty years.²⁹

²² *Skinner v. Northern Trust Co.*, 238 Ill. 229, 123 N. E. 289.

²³ *In re Hanson's Estate*, 38 S. D. 1, 159 N. W. 399.

²⁴ *In re Tone's Will*, 186 N. Y. App. Div. 361, 174 N. Y. Supp. 391.

²⁵ *Georgia v. Cincinnati Southern Ry.*, 248 U. S. 26, 63 L. Ed. 104.

²⁶ *Cross v. Seaboard Air Line R.*

Co., 172 N. C. 119, 90 S. E. 14.

²⁷ *Stevens v. Galveston, H. & S. A. Ry. Co.*, — Tex. —, 212 S. W. 639.

²⁸ *Sisters of Charity of Incarnate Word v. Emery*, 144 La. 614, 81 So. 99.

²⁹ *Sisters of Charity of Incarnate Word v. Emery*, 144 La. 614, 81 So. 99.

VI. PRESUMPTIONS AND COLLATERAL ATTACK

§ 1115. **Collateral attack.**³⁰ An individual in litigation with a corporation cannot take advantage of the fact that the company has not complied with the provisions of the statute with reference to holding real property.³¹

³⁰ See also § 1561, *infra*.

³¹ *Reichert v. Ellis Ferry Co.*,
184 Ky. 150, 211 S. W. 403.

CHAPTER 30

PURCHASE AND OWNERSHIP OF STOCK

I. POWER TO TAKE AND HOLD STOCK IN ANOTHER CORPORATION

§ 1117. General rule—Rule in United States.

§ 1122. Statutory authority.

§ 1125. Effect of purchaser or seller being a foreign corporation.

§ 1126. Taking stock in payment of antecedent debts.

§ 1128. Taking stock as collateral.

§ 1131. Purchase of stock to control corporation.

II. POWER OF CORPORATION TO TAKE AND HOLD ITS OWN STOCK

§ 1135. Rule in United States—Minority rule.

§ 1136. — Majority rule.

§ 1137. Agreement to repurchase stock sold.

§ 1138. Express or implied charter or statutory authority.

§ 1139. Express prohibition or restriction.

§ 1141. Fraud upon or prejudice to creditors or stockholders.

§ 1142. Taking stock as collateral.

§ 1143. Taking stock in payment of debts.

§ 1146. Who may attack.

I. POWER TO TAKE AND HOLD STOCK IN ANOTHER CORPORATION

§ 1117. General rule—Rule in United States. Ordinarily a corporation has no power to purchase stock in another corporation.¹

§ 1122. Statutory authority. Of course a corporation may purchase and hold stock in another corporation where expressly authorized so to do by statute.² Where a statute authorizing the creation of corporations excepts corporations for insurance business, another statute authorizing corporations created under the former statute to purchase stock in other corporations

¹ Central Life Securities Co. v. Smith, 236 Fed. 170; Dillard & Coffin Co. v. Richmond Cotton Oil Co., 140 Tenn. 290, 204 S. W. 758.

² Wrightsville Hardware Co. v. McElroy, 254 Pa. 422, 98 Atl. 1052.

Construction of statutes as to power of bank to buy stock in other corporations, see Moore v. Fremont State Bank, 103 Wash. 249, 173 Pac. 1089.

does not empower a securities company created thereunder to buy stock in an insurance company.³

§ 1125. Effect of purchaser or seller being a foreign corporation. Power to purchase stock in another corporation does not give a foreign corporation the right to own stock in an Illinois corporation.⁴ A consolidated railroad company which becomes thereby a domestic corporation both in Illinois and Indiana, whose road is partly in both states, operates a road connecting with a "railroad of another state," within the Illinois statute, so as to be authorized to purchase stock of the connecting road.⁵

§ 1126. Taking stock in payment of antecedent debts. A corporation may take stock in payment of a debt.⁶

§ 1128. Taking stock as collateral. A corporation may take stock as collateral to secure payment of a loan or performance of a contract.⁷

§ 1131. Purchase of stock to control corporation. The Clayton Act forbidding corporations engaged in commerce to acquire the whole or any part of the stock of another corporation, where the effect will be to lessen competition, does not apply where a subsidiary corporation merely sells the product of the parent company.⁸ The public policy of Illinois will not permit the control of one corporation by another.⁹

II. POWER OF CORPORATION TO TAKE AND HOLD ITS OWN STOCK

§ 1135. Rule in United States—Minority rule. In a few states it is held that a corporation cannot purchase its own stock, with certain exceptions, unless expressly authorized to do so;¹⁰

³ Central Life Securities Co. v. Smith, 236 Fed. 170.

⁴ United Vacuum Sweeper Co. v. Groth, 210 Ill. App. 358.

⁵ Williamson v. Illinois Cent. R. Co., — Ind. App. —, 121 N. E. 324.

⁶ Edwards v. International Pavement Co., 227 Mass. 206, 116 N. E. 266.

⁷ Edwards v. International Pavement Co., 227 Mass. 206, 116 N. E. 266.

⁸ Niles-Bement-Pond Co. v. Iron Molders' Union, 246 Fed. 851.

⁹ United Vacuum Sweeper Co. v. Groth, 210 Ill. App. 358.

¹⁰ Williams v. Maryland Glass Corporation, 134 Md. 320, 106 Atl. 755; Stringfellow v. Rosebrough

but this rule does not prevent a valid gift of its stock to a corporation by a stockholder.¹¹ Such a purchase, although ultra vires, may be ratified by the legislature.¹² The law prohibiting a corporation from purchasing its own stock is not violated by a corporate contract with an employee or officer whereby he is to receive, in addition to a fixed sum, as salary, certain shares of stock to be paid for out of the dividends, but with an option reserved to the corporation to take the stock at par on the officer or employee ceasing to be in the service of the corporation.¹³

On the theory that a corporation cannot do indirectly what it cannot do directly, a corporation, where it has no power to purchase its own stock, cannot agree to resell part of the stock subscribed for and that on a failure to resell the corporation would pay for the stock out of the proceeds of the sale of land conveyed to it by the subscriber in payment for the stock.¹⁴

A surrender of stock to the corporation by stockholders is not invalid as a purchase by the corporation of its own stock, where the stock was not retired but reissued on a sale to other persons.¹⁵

§ 1136. — Majority rule. In most jurisdictions it is held that corporations have power to acquire their own stock.¹⁶ "It is well settled" in the federal courts that a corporation "has inherent power to purchase its own stock."¹⁷ A corporation

Monument Co., — Mo. App. —, 196 S. W. 1050; Whaley v. King, 141 Tenn. 1, 206 S. W. 31.

¹¹ Shaw v. Carr, 93 Wash. 550, 161 Pac. 345.

Where all the stock is transferred for property, surrender of a part of the stock to the corporation to be sold to obtain working capital is not a dealing in its own stock by the corporation. Shaw v. Carr, 93 Wash. 550, 161 Pac. 345.

¹² Brown v. Boston & M. R. R., 233 Mass. 428, 124 N. E. 322.

¹³ Williams v. Maryland Glass Corporation, 134 Md. 320, 106 Atl. 755, construing contract as conditional sale of shares of stock.

¹⁴ Fogarty v. Hunter, 83 Ore. 183, 162 Pac. 964, based on Washington law.

¹⁵ Sargent v. Waterbury, 83 Ore. 159, 161 Pac. 443, 163 Pac. 416.

¹⁶ Sanford v. First Nat. Bank, 238 Fed. 298, Arkansas rule; Farmers' Union Mercantile Co. v. Ricketts, 129 Ark. 177, 195 S. W. 381; Kelly v. McCormick-Murray Mfg. Co., 201 Ill. App. 308; Tapper v. Boston Chamber of Commerce, — Mass. —, 126 N. E. 464; Illoway v. Daly, 65 Pa. Super. Ct. 333; West Texas Supply Co. v. Dunivan, — Tex. Civ. App. —, 198 S. W. 163.

¹⁷ First Trust Co. v. Illinois

may, in Nebraska, turn over real estate or other property to stockholders in exchange for their shares of stock, if done in good faith and not injurious to the rights of creditors or stockholders.¹⁸

§ 1137. Agreement to repurchase stock sold.¹⁹

§ 1138. Express or implied charter or statutory authority. Where a corporation, by its charter, is given power to buy its own stock out of "surplus earnings or accumulated profits," and it does buy its stock and give notes therefor, it must have the surplus at the time the contract is executed and the notes signed and delivered rather than at the time the notes become due.²⁰

In New York, a corporation may purchase its stock only from surplus profits, and where a company had no such surplus the holder of a note given to one selling his stock to the company cannot have his claim allowed as against other creditors.²¹

§ 1139. Express prohibition or restriction.²² In California a corporation cannot purchase its own stock for the reason that the statute prohibits directors from dividing or paying to stockholders any part of the capital stock.²³ The New Jersey statute forbidding declaration of dividends except from surplus or net

Cent. R. Co., 256 Fed. 830. To same effect, see *West Penn Chemical & Manufacturing Co. v. Prentice*, 236 Fed. 891.

Whether a purchase of its own stock is legal depends upon the facts of the particular case. *Sanford v. First Nat. Bank*, 238 Fed. 298.

¹⁸ *Singhaus v. Piper*, 103 Neb. 493, 172 N. W. 523.

¹⁹ See § 604, *supra*.

²⁰ *In re O'Gara v. Maguire*, 259 Fed. 935, and see *In re Feehheim-Fischel Co.*, 212 Fed. 357.

²¹ *Grasselli Chemical Co. v. Aetna Explosives Co.*, 258 Fed. 66.

In re Brueck & Wilson Co., 258 Fed. 69, it was held that such

a note, although valid when issued, was taken at the peril of lack of surplus at the maturity of the note.

²² Delaware statute forbidding purchase by a corporation of its own stock "when such use would cause any impairment of the capital of the corporation" construed. *West Penn Chemical & Manufacturing Co. v. Prentice*, 236 Fed. 891.

²³ *E. J. Dodge Co. v. First Nat. Bank*, 260 Fed. 758, following *Schulte v. Boulevard Gardens Land Co.*, 164 Cal. 464, 44 L. R. A. (N. S.) 156, *Ann. Cas.* 1914 B 1013, 129 Pac. 582.

profits and also the distribution of any part of the capital stock does not prevent a corporation purchasing shares of its own stock, where its capital over and above its capital stock was sufficient to pay existing creditors and also for the stock.²⁴ Under the Nevada statutes forbidding payment to stockholders of any part of the capital stock, or any reduction of capital stock, a corporation cannot purchase its own stock and pay for it out of capital as distinguished from surplus.²⁵ A statute forbidding corporations to purchase or hold their own stock, either absolutely or as collateral, after it has once been issued, does not prevent a company, in its formative stage, contracting for the surrender and cancellation of subscription stock to suppress an overissue in excess of its authorized capitalization, when such correction of the illegal issue is done in good faith, free of any taint of fraud, and not prejudicial to the rights of third persons.²⁶ A statute prohibiting corporations from purchasing their own stock does not make illegal a redemption of preferred stock according to its terms.²⁷

National banks are expressly prohibited from buying their own stock,²⁸ unless necessary to save a debt owing to them.²⁹

§ 1141. Fraud upon or prejudice to creditors or stockholders.³⁰ A purchase of its own stock is invalid where in fraud of creditors,³¹ subject to the limitation that the injury must be to existing creditors, and that subsequent creditors cannot be regarded as prejudicially affected by any such purchase unless

²⁴ *Du Pont v. Du Pont*, 242 Fed. 98, 133.

²⁵ *Jesson v. Noyes*, 245 Fed. 46.

²⁶ *Kelly v. Central Union Fire Ins. Co.*, 101 Kan. 91, L. R. A. 1918 C 1170, 165 Pac. 806.

²⁷ *F. T. Gunther Grocery Co. v. Hazel*, 179 Ky. 775, 201 S. W. 336.

²⁸ *First Nat. Bank v. Armstrong*, 177 Ky. 807, 198 S. W. 226.

²⁹ *First Nat. Bank v. Armstrong*, 177 Ky. 807, 198 S. W. 226; *Commonwealth Trust Co. v. First-Second Nat. Bank*, 260 Pa. 223, 103 Atl. 598.

³⁰ See also § 5057, *infra*.

Purchase of stock in corporation by officers of corporation as conferring rights on corporation, see *Du Pont v. Du Pont*, 256 Fed. 129.

³¹ *Sanford v. First Nat. Bank*, 238 Fed. 298.

A corporation cannot purchase its own stock so as to give the purchaser a claim as a creditor with the right to share equally with other creditors, where the purchase prevents paying other creditors in full and in effect converts stockholders into creditors. *Bayne v. Coming Egg Farm*, — N. J. Eq. —, 111 Atl. 289.

a specific intention is apparent that the purchase was made in anticipation of possible future insolvency.³² Subsequent creditors with notice of the impairment of the capital stock by a purchase by the corporation of its own stock and the execution of bonds to pay therefor, cannot claim priority over the bondholders.³³ There is no fraud where, at the time of the transfer of corporate property to certain stockholders in exchange for their stock, the remaining corporate property is of sufficient value to be ample security for the debts of the corporation.³⁴

If insolvent, a corporation cannot purchase its own stock.³⁵ Where the purchase of its own stock is made when the company is insolvent, or if the purchase renders it insolvent, the sale is voidable as to existing creditors, and if notes or bonds are given by the corporation in exchange for stock, such notes or bonds will be subordinate to the claims of existing creditors in the distribution of the assets of the corporation; and this is also true as to subsequent creditors of the corporation who become such without notice of the purchase but relying upon the previous solvency and unimpaired stock.³⁶

§ 1142. Taking stock as collateral. In Minnesota, a bank taking its own stock as security, must, by statute, sell it within six months; and the time begins to run from the date the stock is acquired. If not so sold, the security is invalid as to creditors or purchasers acquiring rights thereto thereafter from or through the owner of the stock.³⁷

§ 1143. Taking stock in payment of debts. The rule in some states prohibiting a corporation from purchasing its own stock does not apply to a purchase at a sale for unpaid assessments.³⁸ A bank may receive its own stock in payment of a debt although it has no power to purchase its own shares.³⁹

³² *Illoway v. Daly*, 65 Pa. Super. Ct. 333.

³³ *First Trust Co. v. Illinois Cent. R. Co.*, 256 Fed. 830,

³⁴ *Singhaus v. Piper*, 103 Neb. 493, 172 N. W. 523.

³⁵ *Brown v. T. B. Reed Co.*, 31 Idaho 529, 174 Pac. 136.

³⁶ *First Trust Co. v. Illinois Cent. R. Co.*, 256 Fed. 830.

³⁷ *Sigel v. Security State Bank*, 134 Minn. 272, 159 N. W. 567.

³⁸ *Mitchell v. Blue Star Min. Co.*, 98 Wash. 191, 167 Pac. 130.

³⁹ *Noyes v. Wood*, 247 Fed. 72.

§ 1146. Who may attack. If a corporation buys its own stock where it had no authority to do so, it may recover the amount paid, and if insolvent its receiver or assignee may recover.⁴⁰ A stockholder creditor who, with full knowledge of the transfer of corporate property to certain stockholders in exchange for their stock, recognizes it as valid and delays for four years to attack it, is not entitled to relief.⁴¹

⁴⁰ *Whaley v. King*, 141 Tenn. 1,
206 S. W. 31.

⁴¹ *Singhaus v. Piper*, 103 Neb.
493, 172 N. W. 523.

CHAPTER 31

POWERS AS TO FRANCHISES

I. IN GENERAL

§ 1148. Definition and kinds

II. CORPORATE OR GENERAL FRANCHISE

§ 1152. General rules.

III. SPECIAL OR SECONDARY FRANCHISE

§ 1156. General considerations.

§ 1157. Definition and scope.

§ 1158. Distinguished from license.

§ 1160. As including "powers."

§ 1164. Necessity for municipal consent to use of streets.

§ 1165. Exclusive franchises.

§ 1171. Application for and determination of—Imposing conditions.

§ 1172. Acceptance.

§ 1173. Construction.

§ 1174. Duration—In general.

§ 1175. — Where franchise silent.

§ 1178. Forfeiture or revocation—In general.

§ 1179. — As breach of contract.

§ 1180. — Grounds for forfeiture.

§ 1182. — Necessity for declaration of forfeiture or resort to courts.

§ 1183. — Who may assert forfeiture; procedure.

§ 1184. Amendment or modification.

§ 1185. Rights and duties of grantee of franchise.

I. IN GENERAL

§ 1148. Definition and kinds.¹ The "grant, rights, privileges and power to do business of a private corporation are its fran-

¹ Definition of franchise, see *v. Hurlburt*, 83 Ore. 633, 163 Pac. State *v. Black Diamond Co.*, 97 1170.
Ohio St. 24, L. R. A. 1918 E 352, What are franchises, see elaborate discussion in dissenting opinion of Justice Teller in *Grant v. Elder*, 64 Colo. 104, 170 Pac. 198.
119 N. E. 195.

Definition and kinds of franchises, see *Western Union Tel. Co.*

chises.”² Where a statute uses the word “franchise,” it may mean the primary franchise or a secondary franchise. Whether the one or the other depends on the intent of the legislature.³

II. CORPORATE OR GENERAL FRANCHISE

§ 1152. General rules.⁴ A franchise “is a right or privilege granted to a person or corporation by the government or a state either directly or indirectly.” The right “thus granted to an artificial person or legal entity to be a corporation is known as its primary franchise.”⁵ As further illustrating the difference between the primary franchise and other franchises, the Oklahoma court says, in a bank case: “The right to be a corporation and the franchise to conduct business should not be confused. The franchise to do a banking business is controlled by the bank commissioner, subject to statutory regulations. In the event of certain contingencies, defined by statute, such franchise may be withdrawn, but such withdrawal does not destroy the life of the corporation.”⁶

III. SPECIAL OR SECONDARY FRANCHISE

§ 1156. General considerations. An irrigation company to furnish water to raise rice requires no franchise to enable it to do business and hence is not operating a “public utility.”⁷

§ 1157. Definition and scope.⁸ The authority conferred on a corporation “by some sovereign power to transact a particular business or to do a specified act is designated its secondary franchise.”⁹ In Louisiana, secondary franchises are

² Grant v. Elder, 64 Colo. 104, 170 Pac. 198.

³ State ex rel. Coco v. Riverside Irrigation Co., 142 La. 10, 76 So. 216.

⁴ Power to sell, see § 1224, *infra*.

⁵ Western U. Tel. Co. v. Hurlburt, 83 Ore. 633, 163 Pac. 1170.

⁶ First State Bank v. Lee, — Okla. —, 166 Pac. 186.

The right to be a corporation and the franchise to do a bank-

ing business are separate and distinct. First State Bank v. Lee, — Okla. —, 166 Pac. 186.

⁷ State ex rel. Coco v. Riverside Irrigation Co., 142 La. 10, 76 So. 216.

⁸ Definition of “special franchise,” see People v. State Tax Commission, 103 N. Y. Misc. 648, 170 N. Y. Supp. 997.

⁹ Western U. Tel. Co. v. Hurlburt, 83 Ore. 633, 163 Pac. 1170.

defined as "special privileges, in addition to the corporate franchise which may be granted by the state (as the right of eminent domain) or by a parish or municipality (as the right to operate a public ferry, or to make use of a street)." ¹⁰ A grant by the United States to telegraph companies of the right to use highways is a secondary as distinguished from a primary franchise. ¹¹

§ 1158. Distinguished from license. A grant of the right to use streets to a telegraph company is held in Oregon to be a franchise rather than a license. ¹²

§ 1160. As including "powers." ¹³

§ 1164. Necessity for municipal consent to use of streets. ¹⁴ A public service company, although owning abutting property, cannot maintain wires under an alley without the consent of the city as required by statute. ¹⁵

§ 1165. Exclusive franchises. A franchise will not be deemed exclusive unless its terms are clear. ¹⁶ A street railway franchise does not preclude the city building a rival road, without liability for damages. ¹⁷

A statute prohibiting licensing public utilities for duplication of service in any territory, unless a certificate of public

¹⁰ State ex rel. Coco v. Riverside Irrigation Co., 142 La. 10, 76 So. 216.

¹¹ Western U. Tel. Co. v. Hurlburt, 83 Ore. 633, 163 Pac. 1170.

¹² Western U. Tel. Co. v. Hurlburt, 83 Ore. 633, 163 Pac. 1170.

¹³ Right of eminent domain as franchise, see International Smelting Co. v. Tooele County, — Utah —, 182 Pac. 841.

¹⁴ Power of city to compel taking out of franchise to use streets, see Holmes Electric Protective Co. v. Armstrong, 97 N. Y. Misc. 184, 162 N. Y. Supp. 770.

Necessity for street franchise for electric burglar alarm com-

pany, in New York City, see Holmes Electric Protective Co. v. Williams, 228 N. Y. 407, 127 N. E. 315, rev'g 181 N. Y. App. Div. 687, 168 N. Y. Supp. 746.

Right of telephone company to use of streets, see Chesapeake & P. Tel. Co. v. State Roads Commission, 134 Md. 1, 106 Atl. 257.

¹⁵ Holland Realty & Power Co. v. St. Louis, — Mo. —, 221 S. W. 51.

¹⁶ Piedmont Power & Light Co. v. Graham, 253 U. S. 193, 64 L. Ed. 855; North Michigan Water Co. v. Escanaba, 199 Mich. 286, 165 N. W. 847.

¹⁷ United Railroads of San Fran-

necessity is acquired, does not create a monopoly nor is it unconstitutional as impairing the obligation of a contract, or violating the clauses relating to due process, equal protection of the laws, etc.¹⁸

§ 1171. Application for and determination of—Imposing conditions. In granting a franchise to use streets, the municipality may impose any terms it sees fit, except that conditions subsequent must be reasonable.¹⁹ Statutory authority to construct telegraph or telephone lines upon highways or across state bridges does not confer a right to use without compensation.²⁰

§ 1172. Acceptance. A franchise is complete as a contract on the passing of an ordinance and acceptance thereof, before execution of any formal contract.²¹

§ 1173. Construction. In case of doubt, franchise contracts should be construed in favor of the public;²² and no privileges or exemptions will be deemed to have been granted, unless given in clear and explicit terms.²³ But while street franchises are to be strictly construed, they "are not to be so construed as to defeat the purpose for which the grant is made."²⁴ A grant to a railroad of a right of way across highways includes the right to lay water pipes along the right of way.²⁵

cisco v. City and County of San Francisco, 249 U. S. 517, 63 L. Ed. 739, aff'g 239 Fed. 987.

¹⁸ *Farmers' & Merchants' Co. Op. Tel. Co. v. Boswell Tel. Co.*, 187 Ind. 371, 119 N. E. 513.

¹⁹ *Valley Railways v. Mechanicsburg Borough*, 265 Pa. 222, 108 Atl. 629.

²⁰ *American Telephone & Telegraph Co. v. State Roads Commission*, 134 Md. 11, 106 Atl. 260; *Chesapeake & Potomac Tel. Co. v. State Roads Commission*, 132 Md. 194, 103 Atl. 447.

²¹ *Trenton & Mercer County Traction Co. v. Trenton*, 90 N. J. L. 378, 101 Atl. 562.

²² *Piedmont Power & Light Co. v. Graham*, 253 U. S. 193, 64 L. Ed. 855; *City of Dubuque v. Dubuque Elec. Co.*, — Iowa —, 177 N. W. 700; *Cleveland R. Co. v. Cleveland*, 97 Ohio St. 122, 119 N. E. 202.

²³ *Chambersburg v. Chambersburg & G. Elec. Ry. Co.*, 257 Pa. 113, 101 Atl. 922.

²⁴ *State ex rel. Milwaukee Elec. Railway & Light Co. v. Braman*, — Wis. —, 178 N. W. 301.

²⁵ *Louisville & N. R. Co. v. Covington*, 184 Ky. 811, 213 S. W. 568.

§ 1174. Duration—In general.²⁶ While a corporation may take a franchise for a period longer than its corporate existence, a franchise will not be construed as a perpetual one unless in an exceptional case.²⁷ A perpetual franchise is generally held invalid.²⁸ While the Kentucky Constitution prohibits the grants of franchises by cities for more than twenty years, a contract between a city and a public service company extending a few months beyond the twenty years is valid for so much of the period as is embraced within the life of the franchise.²⁹

§ 1175. — Where franchise silent. In some jurisdictions, a franchise not limited in point of time is perpetual.³⁰ In other jurisdictions, if a street franchise is for no definite time, it is limited to the life of the corporation.³¹

§ 1178. Forfeiture or revocation—In general. A franchise partially invalid is not invalid in toto where the good and bad parts are clearly separable.³² Where the remedy for forfeiting a franchise is fixed by the franchise itself, giving power to future councils, the legislative act of the council in revoking the franchise is binding on the courts.³³ Courts cannot relieve a

²⁶ Indeterminate permits, see *State v. Oconto Elec. Co.*, 165 Wis. 467, 161 N. W. 789.

Effect of consolidation of cities on prior franchises, see *Bay City v. Saginaw-Bay City R. Co.*, 207 Mich. 419, 174 N. W. 193.

Perpetual franchises, see note in 2 A. L. R. 1105-1129, annotating *Covington v. South Covington & C. St. R. Co.*, 246 U. S. 413, 62 L. Ed. 802, 2 A. L. R. 1099.

²⁷ *North Michigan Water Co. v. Escanaba*, 199 Mich. 286, 165 N. W. 847.

²⁸ *Newsom v. Rainier*, 94 Ore. 199, 185 Pac. 296.

²⁹ *S. R. Schaff & Co. v. City of La Grange*, 176 Ky. 548, 195 S. W. 1097.

³⁰ See *City of Livingston v. Monidah Trust*, 261 Fed. 966.

A grant of "all the right and authority" that a city "has the capacity to grant" to operate a street railway on certain streets is a grant in perpetuity where the city has authority to make a perpetual grant. *Covington v. South Covington & C. St. R. Co.*, 246 U. S. 413, 62 L. Ed. 802, 2 A. L. R. 1099.

³¹ *People v. Commercial Telephone & Telegraph Co.*, 277 Ill. 265, L. R. A. 1917 D 704, 115 N. E. 379; *Temiskaming Tel. Co., Ltd. v. Town of Cobalt*, 46 Dom. L. Rep. (Can.) 477.

³² *City of La Follette v. La Follette Water, Light & Telephone Co.*, 252 Fed. 762.

³³ *Newsom v. Rainier*, 94 Ore. 199, 185 Pac. 296.

street railway company from a forfeiture of its street franchise incurred by failure to construct the road as provided for in the franchise making it a ground for forfeiture.³⁴

§ 1179. — As breach of contract. Breach of conditions in a street franchise by a gas company is not excused because performance of the conditions was rendered impossible by acts of the federal war board.³⁵

§ 1180. — Grounds for forfeiture. A forfeiture of a street franchise is discretionary with the courts which will hesitate to grant it where it will destroy large investments and no public injury appears.³⁶

§ 1182. — Necessity for declaration of forfeiture or resort to courts. A street franchise is forfeited ipso facto where the ordinance itself provides that it "shall be forfeited" if a certificate of approval is not obtained from the public service commission within a certain time.³⁷

§ 1183. — Who may assert forfeiture; procedure. Forfeiture of a city franchise can be had only by the state or by the city on authority given by the state.³⁸ Parties to a street franchise may contract as to the remedy for noncompliance with the conditions of the franchise, so as to make such remedy exclusive.³⁹

§ 1184. Amendment or modification. The charter right of a telephone company to use highways does not preclude municipal power to direct upon what streets and in what manner the lines shall be installed, so as to prevent a street franchise being based on a consideration and constituting a binding contract.⁴⁰

³⁴ Gas & Electric Securities Co. v. Manhattan & Queens Traction Corporation, 266 Fed. 625.

³⁵ Town of North Hempstead v. Public Service Corp. of Long Island, 107 N. Y. Misc. 19, 176 N. Y. Supp. 621.

³⁶ State ex rel. McAllister v. Cupples Station Light, Heat & Power Co. — Mo. —, 223 S. W. 75.

³⁷ Town of Mill Valley v. National Surety Co., — Cal. App. —, 182 Pac. 459.

³⁸ City of Livingston v. Monidah Trust, 261 Fed. 966.

³⁹ Newsom v. Rainier, 94 Ore. 199, 185 Pac. 296.

⁴⁰ Traverse City v. Citizens' Tel. Co., 195 Mich. 393, 161 N. W. 983.

§ 1185. **Rights and duties of grantee of franchise.** A street franchise is a contract.⁴¹ A purchaser of a railroad at judicial sale has no right to operate it merely for his own private purpose, to the exclusion of the public.⁴² A corporation having a valid street franchise may sue to enjoin interference therewith by a competitor.⁴³ Specific performance of a franchise may be obtained in equity by a public service company, in a proper case.⁴⁴ A street franchise or license to a telephone company gives it no right "to enter upon land within the street and commit acts injurious thereto without the consent of the owner of such land."⁴⁵ Where the conditions in a street railway franchise granted by a city constitute a contract binding the company to construct extensions, the city may compel specific performance of such contract duty.⁴⁶

⁴¹ *State v. Vincennes Traction Co.*, 187 Ind. 291, 117 N. E. 961; *Newcomerstown v. Consolidated Gas Co.*, 100 Ohio St. 494, 127 N. E. 414.

⁴² *State v. Black Diamond Co.*, 97 Ohio St. 24, L. R. A. 1918 E 352, 119 N. E. 195.

⁴³ *Lindsley v. Dallas Consol. St. R. Co.*, — Tex. Civ. App. —, 200 S. W. 207, quoting 4 McQuillin Mun. Corp. § 1771.

⁴⁴ *City of La Follette v. La Follette Water, Light & Telephone Co.*, 252 Fed. 762.

⁴⁵ *Hurlburt v. Union Tel. Co.*, 168 Wis. 125, 169 N. W. 308, trimming trees.

⁴⁶ *Thomas v. Spartanburg Gas & Elec. Co.*, — S. C. —, 103 S. E. 149.

CHAPTER 32

ALIENATION OF PROPERTY AND FRANCHISES

I. GENERAL CONSIDERATIONS

- § 1187. Implied power.
- § 1188. Sale of surplus or of property taken as security.
- § 1193. Transfer for unauthorized purpose or one outside of scope of business—Sale for future delivery.
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- § 1209. — Corporations created to own and sell lands.
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- § 1214. Effect of transfer of all of property.

IV. TRANSFER OF PROPERTY BY QUASI PUBLIC CORPORATIONS

- § 1216. General rules.
- § 1218. Consent of public service commission.
- § 1219. Statutory authority.

V. TRANSFER OF FRANCHISES

- § 1224. Franchise to be a corporation.
- § 1225. Corporate franchises.
- § 1227. Legislative authority.

I. GENERAL CONSIDERATIONS

§ 1187. **Implied power.** Ownership of land by a corporation ordinarily carries with it the power of disposition.¹ A corporation has power to sell property although it had no power to acquire it in the first instance.² A cemetery corporation may sell property to another cemetery corporation, without violating the Missouri statute.³ Power to buy and sell goods includes power to take an order from a customer, send the order to the wholesaler, and have him ship direct to the customer.⁴

§ 1188. **Sale of surplus or of property taken as security.** In Pennsylvania, however, it is held, in construing certain statutes, that a railroad company developing electric current for its own use cannot supply a coal company with current for its mining operations.⁵

§ 1193. **Transfer for unauthorized purpose or one outside of scope of business—Sale for future delivery.**⁶ A cotton gin company has no power to speculate in the cotton seed market by contracting to deliver cotton seed six months in the future, when it did not then own the seed and could not estimate the amount it would take in as a part of the business.⁷ On the other hand, a cotton oil company has power to sell such “linters” as it manufactures, and may “estimate its output for a year, where such estimation is reasonable and made in good faith,” and contract to sell its output on such estimate.⁸

§ 1194. **Property subject to limitations or specified trust.**⁹ Lands held as a cemetery cannot be sold to pay debts or for

¹ Gulf Lines Connecting Ry. v. Golconda Northern Ry., 290 Ill. 384, 125 N. E. 357.

² Sisters of Charity of Incarnate Word v. Emery, 144 La. 614, 81 So. 99; Bishop Mfg. Co. v. Sealy Oil Mill & Manufacturing Co., — Tex. Civ. App. —, 220 S. W. 203.

³ Allison v. Cemetery Caretaking Co., — Mo. —, 223 S. W. 41.

⁴ Sheehan v. Sheehan-Hackley & Co., — Tex. Civ. App. —, 196 S. W. 664.

⁵ Citizens' Electric Illuminating Co. v. Lackawanna & W. V. Power Co., 255 Pa. 176, 99 Atl. 465.

⁶ See also § 847, supra.

⁷ Bishop Mfg. Co. v. Sealy Oil Mill & Manufacturing Co., — Tex. Civ. App. —, 220 S. W. 203.

⁸ Taylor Cotton Oil Co. v. Early-Foster Co., — Tex. Civ. App. —, 204 S. W. 1179.

⁹ Power of religious corporations to sell property, under California statutes, see Giffen v. Christ's

other than cemetery purposes.¹⁰ Trustees of a church to whom land is conveyed for cemetery purposes cannot transfer such land to an oil company to dig for oil.¹¹ Where land was conveyed for a meeting house, burying ground, etc., and the grantee afterwards was incorporated, it could not convey the property for secular uses notwithstanding a general statute conferring power to convey property.¹²

II. SUBSCRIPTIONS, GIFTS AND DONATIONS

§ 1199. Implied power—In general.¹³

§ 1200. — **Donations held beyond corporate power.** A brokerage company has no power to subscribe funds in aid of the erection of a theater building.¹⁴ In Texas, a corporation created for the "raising, buying and selling of live stock" and forbidden by statute to create any debt or "employ its means and assets except for money paid, labor done or property actually received," has no power to execute a note to aid a railroad in constructing its line although it will greatly benefit the land holdings of the live stock company.¹⁵ A charitable corporation cannot donate its funds to another corporation organized for similar or other purposes, unless such donation assists it to carry out the purpose for which the corporation was created.¹⁶

Church, — Cal. App. —, 191 Pac. 718.

For illustration of forfeiture of donation to university where amended charter put it under control of different religious denomination, see *Curtis & Barker v. Central University*, — Iowa —, 176 N. W. 330.

¹⁰ *Hughes v. Pinelawn Cemetery*, — N. Y. Misc. —, 177 N. Y. Supp. 175.

¹¹ *Barker v. Hazel-Fain Oil Co.*, — Tex. Civ. App. —, 219 S. W. 874.

¹² *Chew v. First Presbyterian Church*, 237 Fed. 219.

¹³ For illustration of payment of money by one corporation to another in which it held stock, to relieve it of financial embarrassment, which was held not a gift, see *Howard v. Tatum*, 81 W. Va. 561, 94 S. E. 965.

¹⁴ *Orpheum Theatre & Realty Co. v. Seavey & F. Brokerage Co.*, 197 Mo. App. 661, 199 S. W. 257.

¹⁵ *Richardson v. Bermuda Land & Live Stock Co.*, — Tex. Civ. App. —, 210 S. W. 746.

¹⁶ *Northwestern University v. Wesley Memorial Hospital*, 290 Ill. 205, 125 N. E. 13.

§ 1201. — **Donations held within corporate power.** A corporation has incidental power to create a pension fund to be shared by officers and employees.¹⁷

§ 1202. **Dedication to public use.**¹⁸ A corporation which owns and deals in lands can make dedications;¹⁹ but a public service company cannot dedicate property indispensable to its operation, such as an approach to a bridge.²⁰

III. TRANSFER OF ALL OF PROPERTY

§ 1203. **General rule.** A sale of all the stock of a corporation is in legal effect a sale of all of the assets.²¹ An assignment by a corporation of all its assets "of every kind" includes liability of its directors to it for mismanagement or misconduct.²²

§ 1205. **Power as against creditors.** Under the New York statute permitting one corporation to transfer all its property to another corporation subject to the rights of objecting creditors, a judgment creditor of a foreign corporation which transfers its property all in New York to another foreign corporation may follow such property in the hands of the trustee in bankruptcy of the transferee.²³

§ 1206. **Power as against minority stockholders—In general.**²⁴ A contract of sale of all the corporate assets, providing that it shall not become operative until the owners of all the stock have ratified or signed it, is void where all the stockhold-

¹⁷ *Heinz v. National Bank of Commerce*, 237 Fed. 942, applying rule to a bank.

¹⁸ Power of church to dedicate land, see *Albers v. Acme Paving & Crusher Co.*, 196 Mo. App. 265, 194 S. W. 61.

¹⁹ *Duke Land & Improvement Co. v. Murphy*, 179 N. C. 133, 101 S. E. 497.

²⁰ *Richmond v. Mayo Land & Bridge Co.*, 120 Va. 545, 91 S. E. 615.

²¹ *Johnson v. Canfield-Swigart Co.*, 292 Ill. 101, 126 N. E. 608, aff'g 211 Ill. App. 423.

²² *First Nat. Bank v. Smith*, — W. Va. —, 103 S. E. 318.

²³ *In re American Candy Mfg. Co.*, 256 Fed. 87.

²⁴ "Power of directors to sell property of corporation without consent of stockholders," see note in 5 A. L. R. 930, annotating *Hendren v. Neep*, 279 Mo. 125, 5 A. L. R. 927, 213 S. W. 839.

ers have not signed or ratified.²⁵ A stockholder who participates in a transfer of all the corporate property and who is 'silent when the purchase is proceeding on the theory that the sale had been properly authorized, is estopped to impeach the regularity of the proceedings.²⁶

§ 1207. — Where required by exigencies of business. A majority of the stockholders may sell all the corporate property "when, from any cause, the business of a corporation, not charged with duties to the public, has proved so unprofitable that there is no reasonable prospect of conducting the business in the future without loss, or when the corporation has not, and cannot obtain, the money necessary to pay its debts and to continue the business for which it was organized, even though it may not be insolvent in the commercial sense."²⁷ It "is never ultra vires of a corporation to provide for the payment of its valid debts so far as its assets are available for that purpose," and it may convey all the corporate property to pay debts.²⁸ A majority of the stockholders may sell all the property of an insolvent corporation.²⁹ So a mining corporation may sell all its property when it is in debt and has no money to develop, against the objections of minority stockholders.³⁰ Minority stockholders cannot prevent a sale of all the corporate assets where necessary to prevent the corporation coming to an immediate and disastrous end because the charter was voidable, a change of name was illegal, and under the laws of the territory where operating it would be impossible to carry out necessary contracts.³¹ There is no bad faith in transferring

²⁵ *Williams v. Croft Hat & Notion Co.*, 82 W. Va. 549, 96 S. E. 929.

²⁶ *Akin v. Bates*, 89 Ore. 260, 173 Pac. 889.

²⁷ *Geddes v. Anaconda Copper Min. Co.*, — U. S. —, 65 L. Ed. —, 41 Sup. Ct. 209, rev'g on other grounds 245 Fed. 225, applying rule to sale of silver mine when such mining had become unprofitable.

²⁸ *Bowman v. Anderson*, 268 Mo. 1, 186 S. W. 1012.

²⁹ *Rhea v. Newton*, 262 Fed. 345; *Carrier v. Dixon*, 142 Tenn. 122, 218 S. W. 395, holding also that the 1907 statute is not mandatory; *Beggs v. Myton Canal & Irrigation Co.*, — Utah —, 179 Pac. 984.

³⁰ *Geddes v. Anaconda Copper Min. Co.*, 245 Fed. 225, aff'g 222 Fed. 129, rev'd — U. S. —, 65 L. Ed. —, 41 Sup. Ct. 209.

³¹ *American Elementary Elec. Co. v. Normandy*, 46 App. Cas. (D. C.) 329.

all the property of an irrigation company where necessary because of danger of losing its water rights because of financial trouble.³²

§ 1208. — Where not required by exigencies of business. A solvent corporation cannot sell all its property where a minority stockholder objects.³³

§ 1209. — Corporations created to own and sell lands.³⁴ A corporation authorized by its charter "to purchase and acquire real and personal property and sell and alienate the same, in whole or in part, freely and to the same extent as any person" may do, has power to sell all its property against the dissent of minority stockholders.³⁵ Directors of a company formed to buy and sell real estate may sell a large quantity of land without the consent of all the stockholders.³⁶

§ 1210. — Statutory provisions. Sale of all of the corporate property with the consent of a majority or a certain per cent of the stockholders is often expressly provided for by statute.³⁷ The fact that consent to a sale of all the corporate property was obtained at a directors' meeting, instead of at a stockholders' meeting as required by statute, is immaterial, where the directors either owned or represented all the stock.³⁸ A sale of all the corporate property, even where the consent of the necessary per cent of the stockholders was given at a directors' instead of a stockholders' meeting as required by statute, is at most voidable as distinguished from void.³⁹

In California, all of the corporate property cannot be transferred without the consent of the holders of two-thirds of the

³² *Beggs v. Myton Canal & Irrigation Co.*, — Utah —, 179 Pac. 984.

³³ *Superior Min. Co. v. White Coal Co.*, 214 Ill. App. 381.

³⁴ Construction of charter as to power of real estate company to sell land, see *In re Berry*, 247 Fed. 700.

³⁵ *Logie v. Mother Lode Copper Mines Co.*, 106 Wash. 208, 179 Pac. 835.

³⁶ *Hendren v. Neeper*, 279 Mo. 125, 213 S. W. 839.

³⁷ *Michigan Independent Telephone & Traffic Ass'n v. Michigan Railroad Commission*, 190 Mich. 337, 157 N. W. 52.

³⁸ *In re Drosnes*, 187 N. Y. App. Div. 425, 175 N. Y. Supp. 628.

³⁹ *In re Drosnes*, 187 N. Y. App. Div. 425, 175 N. Y. Supp. 628.

stock; and such consent will not be presumed.⁴⁰ The California statute does not apply to option contracts to purchase, at least where not including the entire business.⁴¹

The Ohio statute requiring notice to stockholders on selling all the corporate property is mandatory, and it is the duty of the purchaser to see that the statute has been fully complied with.⁴²

The Texas statute authorizes corporations to sell or otherwise convey such real and personal estate "as the purposes of the corporation shall require"; and it is held that the directors are the ones to determine when a sale is necessary and that their determination can be attacked only by the state.⁴³

The Utah statute permits mining companies to sell all their property if a majority of the stockholders consent.⁴⁴ In Utah, by statute, all corporations created under the general incorporation law, where a majority of the stockholders agree, may dispose of all the corporate property where there is nothing to the contrary in the articles of incorporation.⁴⁵

§ 1211. Stock of purchasing corporation as consideration.

In some states, a corporation having power to sell all its property and to acquire and own shares of stock in other corporations may sell all its property for stock in another company.⁴⁶ In New Jersey, however, power to sell all the property of the corporation with the consent of the holders of a majority of the stock does not authorize a transfer of all the corporate assets for stock in another corporation to be issued to the several stockholders of the seller, since in violation of the statutes relating to dividends to stockholders from profits and distribu-

⁴⁰ *Porter v. Anglo & London Paris Nat. Bank*, 36 Cal. App. 191, 171 Pac. 845, holding also that sale was void as against execution creditor of the corporation.

⁴¹ *Bradford v. Sunset Land & Water Co.*, 30 Cal. App. 87, 157 Pac. 20.

⁴² *Cyclone Drill Co. v. Zeigler*, 99 Ohio St. 151, 124 N. E. 131.

⁴³ *Gulf Pipe Line Co. v. Lasater*, — Tex. Civ. App. —, 193 S. W. 773.

⁴⁴ *Geddes v. Anaconda Copper Min. Co.*, 245 Fed. 225, aff'g 222 Fed. 129.

⁴⁵ *Beggs v. Myton Canal & Irrigation Co.*, — Utah —, 179 Pac. 984.

⁴⁶ *Logie v. Mother Lode Copper Mines Co.*, 106 Wash. 203, 179 Pac. 835. See *Baker-Matthews Mfg. Co. v. Grayling Lumber Co.*, 134 Ark. 351, 203 S. W. 1021.

tion of capital to stockholders after payment of debts.⁴⁷ So the South Dakota statute authorizing a "sale" of all the corporate assets where authorized by a vote of three-fourths of the stock at a stockholders' meeting, does not apply to a transfer of assets to a corporation organized by the majority stockholders, in exchange for stock in the new company.⁴⁸

The right of a majority of the stockholders to sell all the corporate property, which is generally limited to a sale for cash, includes a transfer for stock in another company which stockholders "may at once, in the New York or other general market, convert into an adequate cash consideration for what his holdings were in the corporate property."⁴⁹

§ 1213. Statutory authorization. Many of the statutes authorizing a sale of all the corporate property apply to and include quasi public corporations.⁵⁰ Where a statute confers power to sell all of the corporate property, it will be presumed that a sale was made under the statute until the contrary affirmatively appears.⁵¹

§ 1214. Effect of transfer of all of property. A sale of all the corporate property does not terminate corporate existence.⁵²

IV. TRANSFER OF PROPERTY BY QUASI PUBLIC CORPORATIONS

§ 1216. General rules. Railroad companies may dispose of terminals to a terminal company.⁵³

⁴⁷ Dalsheimer v. Graphic Arts Co., 86 N. J. Eq. 49, 97 Atl. 497.

⁴⁸ Kremer v. Public Drug Co., 41 S. D. 365, 170 N. W. 571, holding that minority stockholders cannot be compelled to accept stock in another corporation where the corporation transfers all its assets to another corporation for stock.

⁴⁹ Geddes v. Anaconda Copper Min. Co., — U. S. —, 65 L. Ed. —, 41 Sup. Ct. 209, rev'g on other grounds 245 Fed. 225.

⁵⁰ Gulf Pipe Line Co. v. Lasater, — Tex. Civ. App. —, 193 S. W. 773.

⁵¹ Gulf Pipe Line Co. v. Lasater, — Tex. Civ. App. —, 193 S. W. 773.

⁵² Gulf Pipe Line Co. v. Lasater, — Tex. Civ. App. —, 193 S. W. 773.

⁵³ Chicago, M. & St. P. Ry. Co. v. Des Moines Union Ry. Co., 254 Fed. 927.

§ 1218. Consent of public service commission. Statutes requiring consent of the public service commission to sales or leases by public utility corporations are constitutional.⁵⁴ In California, a contract between two electric companies whereby one is to sell out to the other is not enforceable where not approved by the railroad commission.⁵⁵

§ 1219. Statutory authority. The legislature, in the absence of constitutional prohibition, may authorize public service corporations to transfer their franchises and all their property although the transfer may disable them from performing their duties to the public.⁵⁶ Where legislative authority is given to sell all the corporate property, a sale by a quasi public corporation to pay debts is permissible.⁵⁷ Under the Texas statute authorizing corporations to sell their property "as the purposes of the corporation shall require," the property of a quasi public corporation may be sold to pay debts.⁵⁸

Power conferred on a public utility to mortgage property and franchises does not include power to sell.⁵⁹

V. TRANSFER OF FRANCHISES

§ 1224. Franchise to be a corporation. The right to be a corporation is not the subject of barter or sale.⁶⁰

§ 1225. Corporate franchises.⁶¹ A secondary franchise is assignable.⁶² Thus, a franchise to operate a toll bridge may be

⁵⁴ *Central U. Tel. Co. v. Indianapolis Tel. Co.*, — Ind. —, 126 N. E. 628.

⁵⁵ *Napa Valley Elec. Co. v. Calistoga Elec. Co.*, 38 Cal. App. 477, 176 Pac. 699.

⁵⁶ *Gulf Pipe Line Co. v. Lasater*, — Tex. Civ. App. —, 193 S. W. 773.

⁵⁷ *Gulf Pipe Line Co. v. Lasater*, — Tex. Civ. App. —, 193 S. W. 773.

⁵⁸ *Gulf Pipe Line Co. v. Lasater*, — Tex. Civ. App. —, 193 S. W. 773.

⁵⁹ *People ex rel. Pearce v. Com-*

mercial Telephone & Telegraph Co., 277 Ill. 265, L. R. A. 1917 D 704, 115 N. E. 379.

⁶⁰ *Levy v. Reed*, — Okla. —, 170 Pac. 497; *First State Bank v. Lee*, — Okla. —, 166 Pac. 186; *Davis v. Allison*, — Tex. Civ. App. —, 189 S. W. 968.

⁶¹ Note on right to transfer or mortgage privilege to use streets for telegraph, telephone or other quasi public purpose, see L. R. A. 1917 D 707.

⁶² *Traverse City v. Citizens' Tel. Co.*, 195 Mich. 393, 161 N. W. 983.

assigned or sold.⁶³ So a grant of the right to do an intrastate business is a franchise which is assignable as distinguished from the franchise to be a railroad corporation which is not assignable.⁶⁴ If a franchise is granted to a corporation and "its successors and assigns," authority is implied to transfer the franchise; but the rule is to the contrary where the franchise is granted to the corporation alone.⁶⁵ A franchise, such as the right to construct and conduct a railroad, cannot be transferred to an individual for his personal use and not for the public benefit except as the public may receive an advantage, indirectly and remotely, in a commercial way.⁶⁶

§ 1227. Legislative authority. Power to mortgage or lease franchises does not confer authority to sell.⁶⁷

⁶³ *Madison County v. Clay's Ferry Bridge Co.*, 186 Ky. 513, 218 S. W. 299.

⁶⁴ *State v. Roach*, 267 Mo. 300, 184 S. W. 969.

⁶⁵ *People ex rel. Pearce v. Commercial Telephone & Telegraph Co.*, 277 Ill. 265, 270, L. R. A. 1917 D 704, 115 N. E. 379.

⁶⁶ *Bradshaw v. Hilton Lumber Co.*, 179 N. C. 501, 103 S. E. 69.

⁶⁷ *People ex rel. Pearce v. Commercial Telephone & Telegraph Co.*, 277 Ill. 265, L. R. A. 1917 D 704, 115 N. E. 379.

CHAPTER 33

POWERS AS TO LEASES OF PROPERTY

II. POWER TO TAKE OR MAKE LEASE

- § 1231. In general.
- § 1234. Power to take lease.
- § 1235. Power to lease all of property of strictly private corporation.
- § 1236. Power of quasi public corporations—In general.
- § 1237. — Railroad companies.
- § 1239. — Approval by public utility commission.

III. FORM, CONTENTS, VALIDITY AND CONSTRUCTION

- § 1242. Necessity for consent of stockholders.
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- § 1248. Covenants—As to taxes.

IV. ASSIGNMENT OF LEASE OR SUBLETTING

- § 1251. Form, contents and effect.

VI. POWERS, DUTIES, RIGHTS AND LIABILITIES OF LESSOR AND LESSEE

- § 1256. Liabilities of lessor—In general.
- § 1257. — Statutory liability.
- § 1259. — Negligence of lessee.
- § 1262. Rights and liabilities of lessee—Liabilities.

II. POWER TO TAKE OR MAKE LEASE

§ 1231. In general. A corporation created before its enactment is not affected by a statute permitting corporations to lease all their property with the assent of two-thirds in interest of the stockholders.¹

§ 1234. Power to take lease.² A university has power to rent a building to establish a hospital for its medical college.³ Where

¹ Allen v. Francisco Sugar Co., — N. J. Eq. —, 110 Atl. 37. McCray v. Miller, — Okla. —, 184 Pac. 781.

² A mining company is not prohibited from acquiring leases to prospect land for oil and gas, under the Oklahoma Constitution. ³ Ingram v. Texas Christian University, — Tex. Civ. App. —, 196 S. W. 608.

one corporation takes over the property of another company, to ascertain the earning capacity of the latter so as to determine whether it would buy it out, and paid a rental of six per cent of the valuation of the property, the transaction, in effect a lease, was valid.⁴

§ 1235. Power to lease all of property of strictly private corporation. A corporation may lease its property for a limited term of years.⁵ Independently of statute, majority stockholders cannot lease the property where a minority object.⁶ Equity will not sanction a lease of the corporate property in order to escape payment of a million dollars of federal income taxes.⁷ Statutory power to lease all the corporate property with the assent of two-thirds in interest of the stockholders will not be construed as authorizing a lease to a foreign corporation, although the words "any corporation" are used, where the intent seems to be to limit the power to leases to domestic corporations.⁸

§ 1236. Power of quasi public corporations—In general. The contention that a public service company cannot lease its property was answered by the fact that the lease made possible the performance of the principal and important duty for which it was organized.⁹

§ 1237. — Railroad companies.¹⁰ A railroad company has no inherent power to lease its road;¹¹ but a railroad company may lease part of its right of way to promote its business, where not interfering with its duties as a carrier.¹²

⁴ Dillard & Coffin Co. v. Richmond Cotton Oil Co., 140 Tenn. 290, 204 S. W. 758.

⁵ New York Mail & Newspaper Transp. Co. v. Anderson, 234 Fed. 590, 593.

⁶ Allen v. Francisco Sugar Co., — N. J. Eq. —, 110 Atl. 37.

⁷ Allen v. Francisco Sugar Co., — N. J. Eq. —, 110 Atl. 37.

⁸ Allen v. Francisco Sugar Co., — N. J. Eq. —, 110 Atl. 37.

⁹ New York Mail & Newspaper Transp. Co. v. Anderson, 234 Fed. 590, 593.

¹⁰ What are parallel or competing lines, see Chicago, M. & St. P. R. Co. v. Franzen, 287 Ill. 346, 122 N. E. 492.

¹¹ Hampden R. Co. v. Boston & M. R. R., 233 Mass. 411, 124 N. E. 254; Attorney General v. Boston & A. R. Co., 233 Mass. 460, 124 N. E. 257.

¹² Clark v. St. Louis, I. M. & S. R. Co., 132 Ark. 257, 201 S. W. 111.

§ 1239. — **Approval by public utility commission.** Leases of railroads, in Massachusetts, must be approved by the public service commission.¹³

III. FORM, CONTENTS, VALIDITY AND CONSTRUCTION

§ 1242. **Necessity for consent of stockholders.** A lease is an "incumbrance" within the Colorado statute requiring approval of any incumbrance of the property of a mining corporation by a majority of the stock.¹⁴

§ 1244. Construction.¹⁵

§ 1248. **Covenants—As to taxes.** A covenant in a lease to pay all taxes assessed on the premises or business, as distinguished from all taxes imposed on the lessor, does not include the federal income and excess profits tax.¹⁶ But a covenant to pay all taxes for which the lessor would be liable includes the federal income and excess profits taxes although not in existence when the lease was made.¹⁷ An agreement of a railroad leasing terminal facilities to pay "one-third of all taxes or assessments, special or otherwise, and public charges of every kind and nature," made in 1896 before income taxes were anticipated, does not include a duty to pay a third of the income tax exacted from the terminal company.¹⁸

¹³ *Hampden R. Co. v. Boston & M. R. R.*, 233 Mass. 411, 124 N. E. 254.

¹⁴ *Elder v. Western Min. Co.*, 237 Fed. 966.

¹⁵ Construction of railroad lease as to implied guaranty by lessee to pay bonds, etc., which the lessor might issue at the lessee's request, see *Westchester Fire Ins. Co. v. Syracuse, B. & N. Y. R. Co.*, — N. Y. App. Div. —, 183 N. Y. Supp. 602.

Construction of lease of a street railway, where lessee became insolvent and returned the road, as to guaranty fund, see *Westinghouse Elec. & Mfg. Co. v. Brook-*

lyn Rapid Transit Co., 266 Fed. 411.

¹⁶ *Green & Coates Sts. Philadelphia Passenger R. Co. v. Philadelphia Rapid Transit Co.*, 264 Pa. 424, 107 Atl. 784; *Continental Passenger R. Co. of Philadelphia v. Philadelphia Rapid Transit Co.*, 263 Pa. 564, 107 Atl. 390, following *Catawissa R. Co. v. Philadelphia & R. R. Co.*, 255 Pa. 269, 99 Atl. 807.

¹⁷ *Philadelphia City Passenger Ry. Co. v. Philadelphia Rapid Transit Co.*, 263 Pa. 561, 107 Atl. 329.

¹⁸ *Des Moines Union R. Co. v. Chicago Great Western R. Co.*, — Iowa —, 177 N. W. 90.

IV. ASSIGNMENT OF LEASE OR SUBLETTING

§ 1251. Form, contents and effect.¹⁹

VI. POWERS, DUTIES, RIGHTS AND LIABILITIES OF LESSOR AND LESSEE

§ 1256. **Liabilities of lessor—In general.** It is a question for the jury whether a mining company is liable for injuries to an employee after it has leased the mine, as dependent on whether the lease is a mere subterfuge.²⁰

§ 1257. — **Statutory liability.** The legislature may, in permitting leases of railroads to foreign corporations, impose liability for negligence of the lessee on the lessor.²¹ Statutes often make lessors of railroad liable for injuries resulting from the acts of lessees.²² The Missouri statute making the lessor of a railroad jointly liable with its lessee, where the lessee is a foreign corporation, for torts of the lessee in operating the road, does not deprive the lessor of due process of law nor deny the equal protection of the laws.²³

§ 1259. — **Negligence of lessee.**²⁴ The general rule is that a lessor railroad is liable for torts of the lessee in operating the road.²⁵ In Georgia, where, without legislative authority, a railroad company permits another to run cars over its railway, it is liable for any injury done as though the company owning

¹⁹ Service of notice to quit on sublessee, see *F. P. McKay Co. v. Savery House Hotel Co.*, 184 Iowa 260, 168 N. W. 295.

²⁰ *Coal City Min. Co. v. Davis*, — Ala. App. —, 81 So. 358.

²¹ *Murrell v. Kansas City, St. L. & C. R. Co.*, 279 Mo. 92, 213 S. W. 964.

²² *Sorenson v. Chicago, R. I. & P. R. Co.*, 183 Iowa 1123, 168 N. W. 313; *Salley Oil Mill v. Southern Ry.*, 108 S. C. 131, 93 S. E. 336.

²³ *Chicago & A. R. Co. v. McWhirt*, 243 U. S. 422, 61 L. Ed. 826, aff'g — Mo. —, 187 S. W. 830.

²⁴ Note on "Liability of railroad for injuries caused by negligence of another company using the road under a lease, license or other contract," see L. R. A. 1918 E 255.

²⁵ *Morrison v. Hartley*, 178 N. C. 618, 101 S. E. 375; *Bryant v. Sampson Lumber Co.*, 174 N. C. 360, L. R. A. 1918 A 938, 93 S. E. 926; *Mitchell v. Elizabeth River Lumber Co.*, 174 N. C. 119, 93 S. E. 464; *Trinity Valley & N. R. Co. v. Scholz*, — Tex. Civ. App. —, 209 S. W. 224; *Texas & N. O. R. Co. v. Jones*, — Tex. Civ. App. —, 201 S. W. 1085.

the road were itself running the cars.²⁶ In Kentucky the lessor is liable for the negligence of the lessee railroad company.²⁷

Charter power to lease the road to any other railroad company "upon such terms as may be mutually agreed upon" confers no authority to agree as to the respective liabilities of the lessor and lessee to third persons injured by the operation of the road.²⁸

§ 1262. Rights and liabilities of lessee—Liabilities.²⁹ The fact that the occupant of property by permission or as a tenant is a public service corporation does not affect the rule of adverse possession or estoppel to deny the title of the lessor.³⁰

²⁶ *Western U. Tel. Co. v. Spencer*, — Ga. App. —, 101 S. E. 198.

²⁷ *McAllister v. Chesapeake & O. R. Co.*, 243 U. S. 302, 61 L. Ed. 735.

²⁸ *Chicago & A. R. Co. v. McWhirt*, 243 U. S. 422, 61 L. Ed. 826, aff'g — Mo. —, 187 S. W. 830.

²⁹ Lessee as liable for income tax, see *Catawissa R. Co. v. Philadelphia & R. R. Co.*, 255 Pa. 269, 99 Atl. 807, and § 1248, *supra*.

³⁰ *Western U. Tel. Co. v. Louisville & N. R. Co.*, 250 Fed. 199, 206.

CHAPTER 34

MORTGAGES

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II. POWER TO MORTGAGE

§ 1266. Implied power—Corporations other than quasi public corporations. The power to mortgage is only coextensive with the power to alienate absolutely.¹

§ 1269. — As dependent on purpose. A company has no power to execute a mortgage where in effect a mere attempt to lend credit to another company.²

§ 1276. Statutory prohibition or restriction—In general. Restrictions on “transfers” apply to mortgages, since a mortgage is a transfer.³

§ 1277. — Limitations as to amount. A mortgage securing a debt in excess of the statutory limit is binding on the corporation and subsequent creditors.⁴ Judgment creditors whose judgments were obtained after the mortgage was recorded are bound by the mortgage notwithstanding it secures a debt in excess of the statutory limit.⁵

§ 1278. Mortgages to secure debts of officers or stockholders. A mortgage is not invalid merely because it secures the payment of notes indorsed by the directors, especially where no creditors are complaining.⁶

§ 1279. After-acquired property—General rules.⁷ A corporation may mortgage after-acquired personal property.⁸

¹ Gulf Pipe Line Co. v. Lasater, — Tex. Civ. App. —, 193 S. W. 773.

² Taylor Feed Pen Co. v. Taylor Nat. Bank, — Tex. —, 215 S. W. 850.

³ Karasik v. People's Trust Co., 252 Fed. 324, 334.

⁴ Douglass v. State Bank, — Fla. —, 82 So. 593.

⁵ Douglass v. State Bank, — Fla. —, 82 So. 593.

⁶ Freeman v. Mitchell, 206 Mich. 380, 172 N. W. 629, citing Webster v. Ypsilanti Canning Co., 149 Mich. 489, 113 N. W. 7.

⁷ Charter power of railroad company to mortgage after-acquired property, see Southern R. Co. v. Lancaster, 149 Ga. 434, 100 S. E. 380.

⁸ Commercial Trust Co. v. Wertheim Coal & Coke Co., 88 N. J. Eq. 143, 102 Atl. 448.

III. PROPERTY COVERED BY MORTGAGE

§ 1282. General considerations.⁹

§ 1284. **Franchises.** Secondary franchises of railroad companies are subject to mortgage and pass under a foreclosure sale.¹⁰

§ 1285. **General words as covering all the property.** The words "all property" include only such property as is ejusdem generis with that enumerated.¹¹

§ 1288. **After-acquired property—General rules.**¹² Railroad mortgages are somewhat strictly construed in determining whether they cover after-acquired property.¹³ Where a mortgage covers after-acquired property "including particularly" property described, it was held not to cover other property acquired years afterwards.¹⁴

§ 1289. — **Sufficiency of description.** A mortgage covering "real or personal property of every character and description whatsoever constituting additions to and betterments and improvements of the said mortgaged properties," includes after-acquired property of the kind mentioned.¹⁵ Where a mortgage of a company which operated both a water and an ice plant, merely covered the water plant, after-acquired property in the ice plant is not bound thereby.¹⁶

⁹ Machinery put in by a paper company as fixtures, see *In re Russell Falls Co.*, 249 Fed. 260.

¹⁰ *State v. Roach*, 267 Mo. 300, 184 S. W. 969.

¹¹ *United States Cast Iron Pipe & Foundry Co. v. Henry Vogt Mach. Co.*, 182 Ky. 473, 206 S. W. 806.

¹² Construction of mortgage on Venezuela railroad as covering subsequently acquired concessions, see *Baiz v. Coro & L. V. Railroad & Improvement Co.*, 87 N. J. Eq. 438, 101 Atl. 395.

¹³ The "rule is well settled which compels a somewhat strict

construction of these railroad mortgages when ascertaining their effect as equitable mortgages upon after-acquired property." *Baiz v. Coro & L. V. Railroad & Improvement Co.*, 87 N. J. Eq. 438, 101 Atl. 395.

¹⁴ *Westinghouse Elec. Mfg. Co. v. Brooklyn Rapid Transit Co.*, 263 Fed. 532.

¹⁵ *Peoples v. Trust Co. of Georgia*, 256 Fed. 627.

¹⁶ *United States Cast Iron Pipe & Foundry Co. v. Henry Vogt Mach. Co.*, 182 Ky. 473, 206 S. W. 806.

§ 1296. — Property acquired by successor in interest. A mortgage covering after-acquired property does not, on consolidation of the corporation, cover after-acquired property of the other consolidating company.¹⁷ The after-acquired property clause does not cover property acquired in another state by a consolidated company of which the mortgagor became a constituent.¹⁸ The word “successor” as used in an after-acquired property clause in a corporate mortgage does not include an independent corporation which takes title by ordinary purchase.¹⁹

IV. WHO MAY EXECUTE OR AUTHORIZE

§ 1299. Board of directors and other officers.²⁰ The fact that the directors never formally authorized the mortgage is not fatal where they assented to it as stockholders as part of a substantially continuous transaction.²¹ The validity of a mortgage authorized by the directors whose minutes recite and admit the debt secured cannot be attacked on the ground of want of authority of the secretary to execute the notes secured.²²

Where all the three hundred thousand shares of stock except two or three were owned either by the president or his wife, a mortgage executed by the president and not objected to by his wife is binding on the corporation on the theory that the court may look beyond the corporate form and in such a case hold that what would be binding on the persons composing the corporation would be binding on the corporation.²³

§ 1301. Necessity for consent of stockholders. The failure to file the certificate of consent of stockholders, as required by the New York statute, is not fatal where it is clearly shown that all of the stockholders consented.²⁴ The question whether

¹⁷ Metropolitan Trust Co. v. Chicago & E. I. R. Co., 253 Fed. 868.

¹⁸ Railway Steel Springs Co. v. Chicago & E. I. R. Co., 246 Fed. 338.

¹⁹ Mississippi Valley Trust Co. v. Southern Trust Co., 261 Fed. 765.

²⁰ Sufficiency of evidence to show that mortgage was duly authorized by corporation, see People's Trust

Co. v. Mt. Waldo Granite Works, 117 Me. 507, 105 Atl. 113.

²¹ Karasik v. People's Trust Co., 252 Fed. 324, 329.

²² Freeman v. Mitchell, 206 Mich. 380, 172 N. W. 629.

²³ Norma Min. Co. v. Mackay, 241 Fed. 641, and see § 22 et seq., supra.

²⁴ Karasik v. People's Trust Co., 252 Fed. 324, 330.

a corporate mortgage was executed with the consent of stockholders, as required by the New York statute, can be raised not only by the stockholders but also by the corporation and a receiver thereof or by a general assignee for the benefit of creditors.²⁵

V. FORM, CONTENTS, EXECUTION, VALIDITY, ETC.

§ 1302. Form and formal requisites.²⁶

§ 1305. Contents. A mortgage may expressly provide that the mortgagee shall be estopped to deny certain facts, such as the corporate existence of the mortgagor, etc.²⁷

§ 1308. General statutes governing chattel mortgages as applicable.²⁸ In New York, by statute, corporate mortgages on both real and personal property, where duly recorded as a mortgage of real property, need not be filed or refiled as chattel mortgages.²⁹ The New York statute providing that mortgages creating a lien on real and personal property executed by a corporation as security for the payment of bonds, need not be filed as a chattel mortgage, applies to a mortgage securing a single bond.³⁰

§ 1311. Construction in general. A corporate mortgage should be construed not arbitrarily by its terms but with reference to the purposes for which it was made and the objects intended and achieved in its operation.³¹

²⁵ *Leffert v. Jackman*, 227 N. Y. 310, 125 N. E. 446, aff'g *Felbel v. Jackman*, 183 N. Y. App. Div. 938, 169 N. Y. Supp. 1093, following *Vail v. Hamilton*, 85 N. Y. 453.

²⁶ Signature of mortgage, see § 2434 et seq., *infra*.

An instrument held a mortgage rather than an assignment for the benefit of creditors, see *Freeman v. Mitchell*, 206 Mich. 380, 172 N. W. 629.

²⁷ *Southern R. Co. v. Lancaster*, 149 Ga. 434, 100 S. E. 380.

²⁸ Recording mortgage so far as

it covers personalty, see *People's Trust Co. v. Mt. Waldo Granite Works*, 117 Me. 507, 105 Atl. 113.

Sufficiency of affidavit of consideration, see *Commercial Trust Co. v. Wertheim Coal & Coke Co.*, 88 N. J. Eq. 143, 102 Atl. 448.

²⁹ *Karasik v. People's Trust Co.*, 252 Fed. 324, 330.

³⁰ *In re F. & D. Co.*, 256 Fed. 73, following *Clement v. Congress Hall*, 72 N. Y. Misc. 519, 132 N. Y. Supp. 16.

³¹ *Brown v. Pennsylvania R. Co.*, 250 Fed. 513, 518.

§ 1315. Validity—Consideration.³² Where bonds are based on no consideration, the mortgage cannot be sustained as a lien in favor of the original bondholders but only in favor of holders in due course.³³

§ 1317. — Who may attack validity. An officer and stockholder of a corporation who knew of and acquiesced in a corporate mortgage is estopped to sue as a judgment creditor to restrain foreclosure on the ground of illegality of the meeting of the directors at which the mortgage was authorized.³⁴

§ 1319. Recording mortgage.³⁵ The mere recording of a railway mortgage does not create a lien until the consideration has been received by the mortgagor.³⁶

§ 1321. Rights and liabilities of parties.³⁷

VI. RIGHTS AND REMEDIES OF BONDHOLDERS

§ 1324. General rules.³⁸ The rights of bondholders attach from the time the trust deed is executed and the bonds issued and certified by the trustee rather than from the time they pay for the bonds.³⁹

§ 1325. Suit to foreclose—General rules. A provision giving the majority in interest of the bondholders the option to declare

³² Sufficiency of consideration, 541, 103 Atl. 168, rev'g (N. J. Ch.), 102 Atl. 14.
see Robinson v. Phegley, 93 Ore. 299, 182 Pac. 373.

³³ Williamson v. Collins, 243 Fed. 835.

³⁴ Soghomonian v. Garabedian, 231 Mass. 445, 121 N. E. 401.

³⁵ See also § 1308, supra.

³⁶ Sanders v. Southern Traction Co. of Illinois, 253 Fed. 511.

³⁷ Rights of assignee of mortgage, see Robinson v. Phegley, 93 Ore. 299, 182 Pac. 373.

Right of assignee of a mortgage as collateral security to enforce it for payment of debt of mortgagee, see Newark Trust Co. v. Lackawanna Inv. Co., 88 N. J. Eq.

Provision in mortgage as to sinking fund construed so as to make it applicable to payment of principal of bonds before payment of interest, see Brown v. Pennsylvania R. Co., 250 Fed. 513.

³⁸ Estoppel of bondholders to deny responsibility on contract made pending foreclosure, where enhancing value of property, see Stokes v. Newark Meadows Improvement Co., 90 N. J. Eq. 185, 106 Atl. 132.

³⁹ Welch v. Northern Bank & Trust Co., 100 Wash. 349, 170 Pac. 1029.

the principal of the bonds due does not prevent a foreclosure by minority bondholders for nonpayment of interest.⁴⁰ Bondholders, by their acts, may waive the right to demand a foreclosure because of default in payments, as against a lessee of the property, where the lease was made at a time when a default existed, notwithstanding the trustee did not join in the lease as required by the deed of trust.⁴¹ Laches may bar the right of bondholders to foreclose.⁴² The trustee is not a necessary defendant, where he refuses to act, in an action by bondholders to foreclose the mortgage.⁴³

Bondholders who successfully sue to foreclose the mortgage, on the trustee refusing to act, are entitled to recover costs and disbursements, although claims as to the rights of other bondholders and the extent of the lien were denied.⁴⁴

§ 1326. — Necessity for refusal of trustee to sue. A bondholder may sue to foreclose, without first requesting the trustee to act as required by the mortgage, where it would be a useless act.⁴⁵

§ 1327. — Joinder of all bondholders. In a foreclosure suit brought by part of the bondholders, the court may order holders of other bonds secured by the same mortgage to be made defendants.⁴⁶

§ 1328. — Effect of provisions in mortgage. A provision in the mortgage in effect barring the right of minority bondholders to sue to foreclose is void as ousting the jurisdiction of the courts.⁴⁷ A provision giving the majority bondholders the option to declare the principal of the bonds due does not prevent a foreclosure for interest by a minority bondholder.⁴⁸ The

⁴⁰ *Brown v. Denver Omnibus & Cab Co.*, 254 Fed. 560.

⁴¹ *Oberman v. Red Rock Fuel Co.*, 83 W. Va. 531, 99 S. E. 66.

⁴² *Southern R. Co. v. Lancaster*, 149 Ga. 434, 100 S. E. 330.

⁴³ *Brown v. Denver Omnibus & Cab Co.*, 254 Fed. 560.

⁴⁴ *Wegner v. Sheboygan-Elkhart Lake Ry. & Elec. Co.*, — Wis. —, 176 N. W. 865.

⁴⁵ *Brown v. Denver Omnibus & Cab Co.*, 254 Fed. 560.

⁴⁶ *Wegner v. Sheboygan-Elkhart Lake Ry. & Elec. Co.*, — Wis. —, 176 N. W. 865.

⁴⁷ *Brown v. Denver Omnibus & Cab Co.*, 254 Fed. 560.

⁴⁸ *Brown v. Denver Omnibus & Cab Co.*, 254 Fed. 560.

fact that a mortgage provides for foreclosure only upon request of a majority of the bondholders does not preclude a suit to foreclose by a minority bondholder where a majority of the bondholders had conspired with the mortgagor to defraud.⁴⁹ A party "holding defaulted bonds as collateral for the security of his debt is, to the extent of his debt at least, subrogated to such an interest in the property, mortgaged to secure the bonds, as will enable him to require the trustee, when the mortgage authorizes it, to foreclose the mortgage for the payment of the debt." ⁵⁰

§ 1330. Actions against mortgagor or third persons. Bondholders cannot sue to protect the mortgaged property unless the mortgage trustee refuses to sue.⁵¹

VII. TRUSTEES

§ 1334. Filling vacancies. The mode of appointment of a substituted trustee is often expressly provided for by the deed of trust.⁵²

§ 1335. Removal, disqualification and resignation. A mortgage trustee should not be removed merely because he has acted beyond his powers, in the absence of bad faith on his part, unless some benefit to the trust can be accomplished thereby.⁵³

§ 1336. Nature of office—General rules. The trustee is the common agent of both parties and must act impartially.⁵⁴

§ 1337. — Trustee as representing bondholders. Consent of a mortgage trustee to the issuance of receiver's certificates is binding on the bondholders.⁵⁵ Holders of bonds, represented

⁴⁹ *Brown v. Denver Omnibus & Cab Co.*, 254 Fed. 560.

⁵⁰ *People's Trust Co. v. Mt. Waldo Granite Works*, 117 Me. 507, 105 Atl. 113.

⁵¹ *Winthrop v. Fellows*, 230 Fed. 702, 705, suit to enjoin enforcement of rate statute against railroad company.

⁵² *West v. Union Naval Stores Co.*, 117 Miss. 153, 77 So. 961.

⁵³ *Conover v. Guarantee Trust Co.*, 88 N. J. Eq. 450, 102 Atl. 844.

⁵⁴ *Ainsa v. Mercantile Trust Co.*, 174 Cal. 504, 163 Pac. 898.

⁵⁵ *Pillinger v. Beaty*, 265 Fed. 551.

by the mortgage trustee, are bound by a decree declaring the bonds void.⁵⁶

§ 1339. Powers—In general. A trustee given power to certify bonds of a corporation when mortgages are assigned to it by the trustee has no authority to certify bonds secured by mortgages executed by the corporation itself.⁵⁷

§ 1344. — Power to sue. A trust company, acting as trustee of railroad bonds pledged to secure an issue of short term notes, has no such interest as to entitle it to attack the validity of a subsequent pledge of other bonds of the same issue.⁵⁸

§ 1345. Duties—General rules.⁵⁹ The trustee owes a duty to the bondholder of preservation and protection of the security, if the means of defense are known to him or may with diligence be discovered.⁶⁰

A trust company, acting as mortgage trustee, cannot divide itself into units or parts, so as to escape imputation of knowledge possessed by the banking department, through its paying teller, that defaults had been made in payment of interest on the mortgage.⁶¹

§ 1349. Personal liability—In general.⁶² There is no liability for mere error of judgment.⁶³ Errors of judgment, however, are

⁵⁶ *In re Franklin Brewing Co.*, 254 Fed. 910.

⁵⁷ *Conover v. Guarantee Trust Co.*, 88 N. J. Eq. 450, 102 Atl. 844.

⁵⁸ *Central Trust Co. v. Missouri, K. & T. R. Co.*, 247 Fed. 586.

⁵⁹ Trustee held to assume the obligations of a trustee of an "active" rather than a "dry" trust, see *Welch v. Northern Bank & Trust Co.*, 100 Wash. 349, 170 Pac. 1029.

Trustee in particular case held to have acted properly in retiring certain bonds for the benefit of the sinking fund, see *Estabrook v. International Trust Co.*, 227 Mass. 281, 116 N. E. 486.

Liabilities in general, see *Welch v. Northern Bank & Trust Co.*, 100 Wash. 349, 170 Pac. 1029.

Measure of damages for acts of trustee, see *Conover v. Guarantee Trust Co.*, 88 N. J. Eq. 450, 102 Atl. 844.

⁶⁰ *Ainsa v. Mercantile Trust Co.*, 174 Cal. 504, 163 Pac. 898.

⁶¹ *Browning v. Fidelity Trust Co.*, 250 Fed. 321.

⁶² Liability of trustee in general, see *Ainsa v. Mercantile Trust Co.*, 174 Cal. 504, 163 Pac. 898.

⁶³ *Conover v. Guarantee Trust Co.*, 88 N. J. Eq. 450, 102 Atl. 844.

to be distinguished from acts wholly unauthorized by the deed of trust.⁶⁴

Corporate trustees are generally relieved by the terms of the mortgage from liability except for gross negligence or bad faith.⁶⁵ Immunity clauses in deeds of trust do not cover acts clearly beyond the scope of the trustee's power.⁶⁶

§ 1352. — Use of bonds, proceeds or other moneys.⁶⁷

§ 1354. — Effect of certificates on bonds.⁶⁸

§ 1356. Compensation and reimbursement. Compensation should be denied a mortgage trustee who acts in bad faith.⁶⁹ The trustee will be denied compensation for bringing the foreclosure suit where it, through control of the board of directors of the mortgagor, conducts the corporate affairs to the loss of the corporation and to its gain.⁷⁰

VIII. FORECLOSURE BY SUIT

§ 1357. General rules. Consent of the public service commission is not necessary to authorize foreclosure of a street railway mortgage.⁷¹

§ 1360. Necessity for and sufficiency of request of bondholders to sue. Provisions in a deed of trust requiring a concurrence of one-third of the bondholders in requesting a fore-

⁶⁴ Conover v. Guarantee Trust Co., 88 N. J. Eq. 450, 102 Atl. 844.

⁶⁵ Browning v. Fidelity Trust Co., 250 Fed. 321, where trust company, in releasing portions of the mortgaged premises, was held not liable because negligence was not gross and there was no bad faith.

⁶⁶ Conover v. Guarantee Trust Co., 88 N. J. Eq. 450, 102 Atl. 844.

Liability of trustee for failure to enforce covenant of mortgagor in the mortgage as to fire insurance, as barred by express covenant, see Bell v. Scranton Trust Co., 261 Pa. 28, 103 Atl. 1019.

⁶⁷ Delivery of bonds as negligence, see Reynoldsville Water Co. v. Farmers' & Miners' Trust Co., 257 Pa. 341, 101 Atl. 800.

⁶⁸ See § 994, supra.

⁶⁹ Title Insurance & Trust Co. v. Northwestern Long-Distance Tel. Co., 88 Ore. 666, 173 Pac. 251.

⁷⁰ Title Insurance & Trust Co. v. Northwestern Long-Distance Tel. Co., 88 Ore. 666, 173 Pac. 251.

⁷¹ Philadelphia Trust Co. v. Northumberland County Traction Co., 258 Pa. 152, 101 Atl. 970.

closure and also requiring the bondholders to indemnify the trustee as to expenses, etc., do not apply where one person owns the entire bond issue.⁷² A provision in a trust deed requiring "a demand by twenty-five per cent in value of the bondholders" to move the trustee to action, restricts collection or foreclosure proceedings, but is not a limitation upon the inherent rights of bondholders to protect their interests as by an injunction suit.⁷³

§ 1361. Injunction against foreclosure.⁷⁴ On default, foreclosure of a corporate mortgage cannot be enjoined without impairing the obligation of a contract.⁷⁵ The existence of a receivership does not warrant an injunction restraining foreclosure where interest is in default.⁷⁶

§ 1363. What constitutes default—Default in payments.⁷⁷ Presentation of interest coupons is necessary before bondholders can elect to declare the whole debt due for nonpayment of interest where they had agreed not to present the coupons for payment until after a certain date.⁷⁸

§ 1368. Jurisdiction—Of federal courts. A federal court has jurisdiction of a suit by a bondholder to foreclose the mortgage although the mortgage trustee made a defendant is a citizen of the same state as the plaintiff, where the mortgagor is a citizen of a different state.⁷⁹

§ 1371. Parties—Plaintiff or plaintiffs.⁸⁰

⁷² *Southern Nat. Bank v. Germania Mfg. Co.*, 176 N. C. 318, 97 S. E. 1.

⁷³ *Hoyt v. E. I. Du Pont De Nemours Powder Co.*, 88 N. J. Eq. 196, 102 Atl. 666.

⁷⁴ Estoppel to enjoin foreclosure suit, see *Parks v. Hughes*, 145 La. 221, 82 So. 202.

⁷⁵ *Philadelphia Trust Co. v. Northumberland County Traction Co.*, 258 Pa. 152, 101 Atl. 970.

⁷⁶ *Westinghouse Elec. & Mfg. Co. v. Binghamton Ry. Co.*, 255 Fed. 378.

⁷⁷ What constitutes default in payment, see *Mercantile Trust Co. v. Sunset Road Oil Co.*, 176 Cal. 461, 168 Pac. 1037.

⁷⁸ *Metropolitan Trust Co. of City of New York v. Long Acre Elec. Light & Power Co.*, 184 N. Y. App. Div. 156, 171 N. Y. Supp. 557.

⁷⁹ *Brown v. Denver Omnibus & Cab Co.*, 254 Fed. 560.

⁸⁰ That person who owns all the bonds may sue to foreclose, see *Southern Nat. Bank v. Germania Mfg. Co.*, 176 N. C. 318, 97 S. E. 1.

§ 1372. — **Defendant or defendants.** Representatives of the corporate mortgagor, dissolved by insolvency, are necessary parties to the foreclosure suit.⁸¹

§ 1373. **Intervention—General rules.**⁸² The state may be permitted to intervene in a suit to foreclose a mortgage on a railroad, where the result contemplated will be discontinuance of the road.⁸³

§ 1374. — **Bondholders.** A bondholder is entitled to intervene in a foreclosure suit, in a proper case.⁸⁴

§ 1375. — **Stockholders.** A stockholder cannot appear as a defendant in a foreclosure suit against a corporation but must petition to intervene.⁸⁵ Stockholders cannot intervene because of failure of the corporation to set up defenses, where they made no demand on the corporation to so act.⁸⁶ Intervening stockholders cannot raise the question as to whether some of the stockholders had paid for the stock held by them.⁸⁷

§ 1376. — **Creditors other than bondholders and other third persons.** Under the Idaho statutes, judgment and general creditors may intervene.⁸⁸

§ 1378. **Defenses—Want or failure of consideration.** If, in a foreclosure suit, the corporation claims the bonds are void for failure of consideration, the burden is on it to prove the failure of consideration.⁸⁹

⁸¹ *Leyhe v. Leyhe*, — Tex. Civ. App. —, 220 S. W. 377.

⁸² Right to intervene in foreclosure suit, see *Anam Realty Co. v. Delancey Garage*, 190 N. Y. App. Div. 745, 180 N. Y. Supp. 297.

⁸³ *Hood v. Ocklawaha Valley R. Co.*, — Fla. —, 84 So. 97.

⁸⁴ *Walpole v. Rogers*, — Colo. —, 185 Pac. 346.

⁸⁵ *Mercantile Trust Co. of San Francisco v. Stockton Terminal & E. R. Co.*, — Cal. App. —, 186 Pac. 1049.

⁸⁶ *Rospigliosi v. New Orleans, M. & C. R. Co.*, 237 Fed. 341.

⁸⁷ *Fidelity Trust Co. v. Elberton & E. R. Co.*, 235 Fed. 1009.

⁸⁸ *Equitable Trust Co. v. Great Shoshone & Twin Falls Water Power Co.*, 245 Fed. 697, aff'g 228 Fed. 516.

⁸⁹ *Stevens v. Ottumwa Cold Storage & Ice Co.*, 182 Iowa 854, 166 N. W. 282.

§ 1380. — **Matters relating to default in payment.** It is no defense to a foreclosure suit that the reason for default in paying interest is that the trustee, acting with the directors, has so manipulated the corporate affairs that the corporation is unable to pay the interest.⁹⁰

§ 1382. — **By persons other than the mortgagor.** An execution purchaser of railroad property may contest the validity of an alleged prior mortgage thereon where foreclosure is sought.⁹¹

§ 1385. **Decree—General rules.** The foreclosure decree must be in favor of both assenting and nonassenting bondholders so far as a lease of the premises subject to the mortgage is concerned.⁹² In a foreclosure suit, where the mortgagee was a stockholder, the decree cannot award an assessment of his stock for an unpaid balance in favor of the trustee in bankruptcy of the mortgagor.⁹³

A mortgage trustee is entitled to a deficiency decree where the trust deed expressly authorizes him to collect any deficiency in his own name.⁹⁴ The trustee of a mortgage securing bonds, on foreclosure, cannot, as such trustee, recover a deficiency judgment unless the mortgage gives him such right.⁹⁵ While it seems that a mortgage trustee may file a claim in bankruptcy for a deficiency judgment, as representing the bondholders, the court may permit an amendment filed by the bondholders ratifying the acts of their trustee and making the claim a direct one.⁹⁶

§ 1387. — **Provisions as to sale.** On foreclosing a mortgage on a street railroad, where it is not clear that the road cannot be operated without loss, the court may order its sale as a going concern for a fixed price, and if such price is not offered require the receiver to operate it for one year to see if it can be operated without loss, and if it cannot be operated without loss order it

⁹⁰ Title Insurance & Trust Co. v. Northwestern Long-Distance Tel. Co., 88 Ore. 666, 173 Pac. 251.

⁹¹ Stewart v. Florida, G. & W. Ry. Co., 255 Fed. 616.

⁹² Mercantile Trust Co. v. Sunset Road Oil Co., 176 Cal. 461, 168 Pac. 1037.

⁹³ Myers v. Indiana Min. Co., 86 Ore. 664, 168 Pac. 719.

⁹⁴ Lane v. Equitable Trust Co., 262 Fed. 918.

⁹⁵ Brant Independent Min. Co. v. Palmer, 262 Fed. 370.

⁹⁶ In re A. J. Ellis, Inc., 252 Fed. 483.

sold for junk and permit the company to abandon its permissive franchise.⁹⁷

§ 1392. — Effect as res judicata or bar. The foreclosure decree binds holders of receivers' certificates as to priorities where they intervened after final decree.⁹⁸ Bondholders may, by the terms of a decree instructing the mortgage trustee, be declared bound thereby where due notice had been given all of them.⁹⁹ Where the court had no jurisdiction of the property in a foreclosure suit, the decree is not binding on subscribers to the bonds who had repudiated their subscriptions and were not made parties to the suit.¹

§ 1394. — Vacating or setting aside.²

§ 1395. Sale—In general.³ Railroad property may be severed into parcels for purpose of foreclosure sales.⁴

§ 1396. — Who may purchase. Majority stockholders who are also chief officers of the company may, as bondholders and creditors of the company, on the insolvency of the company, purchase the property at foreclosure sale, where they were not the cause of the insolvency, the sale was not procured by their acts, they had no duty to perform at the sale, and they acted in good faith.⁵

§ 1397. — Bids. Requiring bidders to deposit a certain sum of money or a certified check or a certain number of bonds does not prevent competitive bidding so as to avoid the sale.⁶

⁹⁷ *Potter Matlock Trust Co. v. Warren County*, 182 Ky. 840, 207 S. W. 709.

⁹⁸ *American Nat. Bank v. Lamb*, 147 Ga. 667, 95 S. E. 227.

⁹⁹ *United States Mortgage & Trust Co. v. New York Dock Co.*, 108 N. Y. Misc. 120, 177 N. Y. Supp. 455.

¹ *Columbia-Knickerbocker Trust Co. v. Abbot*, 247 Fed. 333.

² Grounds for when new trial granted in favor of some of the

bondholders, see *Mercantile Trust Co. v. Sunset Road Oil Co.*, 176 Cal. 451, 168 Pac. 1036.

³ Sale as judicial sale, see *Com. v. Keystone Graphite Co.*, 257 Pa. 249, 101 Atl. 766.

⁴ *Metropolitan Trust Co. v. Chicago & E. I. R. Co.*, 253 Fed. 868.

⁵ *Sebree v. Cassville & W. R. Co.*, — Mo. —, 212 S. W. 11.

⁶ *Rospigliosi v. New Orleans, M. & C. R. Co.*, 237 Fed. 341.

§ 1400. — Confirmation of sale.⁷

§ 1402. — Setting sale aside.⁸ Failure of the corporation to make any defense in the foreclosure suit does not show collusion or fraud warranting the setting aside of the sale.⁹ After confirmation of the sale it cannot be set aside merely because of inadequacy of price nor offers of better prices, but only for fraud or the like for which equity would avoid a like sale between individuals.¹⁰ A creditor of a corporation who is present at the sale and makes no objections at such time nor to its confirmation cannot have it set aside a year later on the ground that the purchasers had no power to purchase.¹¹

§ 1403. Title, rights and liabilities of purchaser—In general. If a director purchases at a foreclosure sale he takes with notice of defects in the bonds, where all the facts were known.¹²

§ 1404. — Liability for debts and claims. Foreclosure sale cuts off claims of unsecured creditors and of subsequent lienors.¹³ A purchaser at foreclosure sale is not liable for a breach of contract by the mortgagor unless the decree so provides.¹⁴ A sale by a mortgage trustee under a power of sale is not a judicial sale so as to divest a lien for state taxes.¹⁵

§ 1406. — Duties of purchaser. The foreclosure purchaser of a railroad takes it burdened with the duty to operate it, and this duty cannot be avoided by a vacation order modifying the foreclosure decree.¹⁶

⁷ Confirming a foreclosure sale without an order nisi held no ground for setting aside the confirmation in *Painter v. Union Trust Co.*, 246 Fed. 240.

⁸ Inadequacy of price, on sale of railroad, as ground for setting sale aside, see *Rospigliosi v. New Orleans, M. & C. R. Co.*, 237 Fed. 341.

See also *Freeman v. Mitchell*, 206 Mich. 380, 172 N. W. 629.

⁹ *Rospigliosi v. New Orleans, M. & C. R. Co.*, 237 Fed. 341.

¹⁰ *Sebree v. Cassville & W. R. Co.*, — Mo. —, 212 S. W. 11.

¹¹ *Sebree v. Cassville & W. R. Co.*, — Mo. —, 212 S. W. 11.

¹² *Hess Warming & Ventilating Co. v. Burlington Grain Elevator Co.*, — Mo. —, 217 S. W. 493.

¹³ *Male v. Atchison, T. & S. F. R. Co.*, 179 N. Y. App. Div. 87, 166 N. Y. Supp. 593.

¹⁴ *Brown v. Western Maryland R. Co.*, 82 W. Va. 511, 96 S. E. 799.

¹⁵ *Com. v. Keystone Graphite Co.*, 257 Pa. 249, 101 Atl. 766.

¹⁶ *State v. Beaton*, — Iowa —, 178 N. W. 1.

§ 1407. — **Contracts as binding on purchaser.**¹⁷ Foreclosure and sale of a railroad in a federal court will not relieve the purchaser from a contractual or statutory duty, resting on its predecessors under the state law, to maintain offices and shops at a particular place, if the state law holds the obligation indelible by foreclosure.¹⁸

§ 1408. — **Statutory liability.**¹⁹

§ 1411. — **Suits by purchaser.** On foreclosure sale, the purchaser cannot dispossess the mortgagor, a public service company, of a part of its plant necessary for service to the public, where the purchaser has no franchise to render the same service.²⁰

IX. DISTRIBUTION OF PROCEEDS; PRIORITIES

§ 1414. **Application of proceeds—General rules.**²¹ A mortgage given by a corporation to secure the redemption of preferred stock is valid as a prior lien as against claims of common stockholders.²² Where a bond issue is owned by stockholders, the interest as bondholders is merged in their interest as stockholders, so far as priority against other creditors on foreclosure is concerned.²³ Stockholders in possession of bonds issued to them as a bonus, while they cannot compete as creditors, are in a position analogous to that of first preferred stockholders so that all the company's funds which could be legally devoted to the payment of dividends, and, on liquidation, to distribution among stockholders, should be first applied to their claims.²⁴

¹⁷ Construction of foreclosure decree giving purchaser option to adopt or repudiate executory contracts of railway company, the mortgagor, see *Wichita Union Terminal R. Co. v. Kansas City, M. & O. R. Co.*, 105 Kan. 262, 182 Pac. 535.

¹⁸ *International & G. N. R. Co. v. Anderson County*, 246 U. S. 424, 62 L. Ed. 807, aff'g — *Tex. Civ. App.* —, 174 S. W. 305.

¹⁹ See § 1437, *infra*.

²⁰ *Lowe v. Los Angeles Subur-*

ban Gas Co., — Cal. —, 189 Pac. 1084.

²¹ Whether person a creditor or investor, on distributing proceeds of foreclosure, see *Phillips v. Pine Bluff, S. & S. R. Co.*, 137 Ark. 443, 208 S. W. 313.

²² *Hewitt v. Linnhaven Orchard Co.*, 90 Ore. 1, 174 Pac. 616.

²³ *First Trust Co. v. Crooked Creek Railroad & Coal Co.*, 243 Fed. 450.

²⁴ *Williamson v. Collins*, 243 Fed. 835.

§ 1417. Priorities as between interest and principal.²⁵

§ 1421. Priorities as between mortgage and other liens or claims—In general.²⁶ One loaning money to an embarrassed corporation and taking security therefor is not entitled to priority over prior mortgages.²⁷ A general manager of a mine cannot acquire a lien for services as against bondholders.²⁸

§ 1429. Priorities as to after-acquired property—General rule. In the case of public service corporations, property acquired after the mortgage and covered thereby, "and which composes an integral, indispensable or necessary part of its machinery or fixtures, to perform things which it is empowered by its articles of incorporation to do, are covered by lien of the mortgage, not only as between the mortgagor and mortgagee, but as between the mortgagee and subsequent purchasers and claimants of liens. * * * Otherwise the general rule prevails, which is that the lien of the mortgage, where it provides for a lien upon after-acquired property, attaches to the after-acquired property in the condition in which it is at the time it comes into the hands of the mortgagor, as to prior liens, and the general mortgage does not displace such liens, although they may be junior." ²⁹

§ 1435. Priorities as affected by statutes—General rules.³⁰ Under the Illinois statutes, the lien of contractors constructing a railroad is superior to that of a previously recorded mort-

²⁵ On this question, see *Brown v. Pennsylvania Canal Co.*, 244 Fed. 980.

²⁶ Claim of director for money advanced to pay for and improve after-acquired property held superior to lien of mortgage in *Skelly v. Jamaica Bay Mfg. Co.*, 182 N. Y. App. Div. 201, 169 N. Y. Supp. 516.

²⁷ *Andrews Institute for Girls v. New York Steam Co.*, 266 Fed. 872.

²⁸ *International Trust Co. v. Lowe*, — Colo. —, 180 Pac. 579.

²⁹ *United States Cast Iron Pipe & Foundry Co. v. Henry Vogt Mach. Co.*, 182 Ky. 473, 206 S. W. 806.

³⁰ Statutory liens in Georgia entitled to priority, see *Baltimore Trust Co. v. Seaboard Air Line R. Co.*, 149 Ga. 260, 99 S. E. 867; *Baltimore Trust Co. v. Western U. Tel. Co.*, 149 Ga. 262, 99 S. E. 868.

Statutory lien for wages as prior to mortgage, see *Valdosta, M. & W. R. Co. v. Atlantic Coast Line R. Co.*, 148 Ga. 842, 98 S. E. 465.

gage given to secure railroad bonds.³¹ Statutes ordinarily do not give claims any priority over purchase money mortgages.³² Supplying of cars for a railroad is "furnishing of material, supplies or other articles" within the statute awarding priority to such claims for six months, as against a mortgage.³³

§ 1437. — Judgments for torts or labor. A statute providing that no railroad lien shall be valid against judgments for damages in the operation of the road, is constitutional.³⁴ The statutory priority given a judgment for damages to property by a railroad company, as against a prior mortgage, extends to the property in the hands of the foreclosure purchaser.³⁵ In North Carolina, a judgment against a corporation for a tort is entitled to priority as against a subsequent deed of trust only where an action to enforce such judgment is brought within sixty days after the registration of the deed of trust.³⁶ The statute "simply wipes out the mortgage as against a judgment for tort, so that the judgment creditor may proceed to collect his judgment as if there was no mortgage, by execution if the property is not in the hands of a receiver, or by prorating with the mortgage creditors if a receiver has taken charge."³⁷ A judgment against a railroad for personal injuries is not a prior lien over a mortgage given before the injury, under the Michigan statutes.³⁸

§ 1440. Who may question priority.³⁹

³¹ Sanders v. Southern Traction Co. of Illinois, 253 Fed. 511.

³² Humphrey Bros. v. Buell-Crocker Lumber Co., 174 N. C. 514, 93 S. E. 971.

³³ Valdosta, M. & W. R. Co. v. Atlantic Coast Line R. Co., 148 Ga. 842, 98 S. E. 465.

³⁴ Petition of Walker, — Tenn. —, 209 S. W. 739.

³⁵ Henry Mercantile Co. v. Graham, 108 S. C. 125, 93 S. E. 331.

³⁶ Joyner v. Reflector Co., 176 N. C. 274, 97 S. E. 44.

³⁷ Joyner v. Reflector Co., 176 N. C. 274, 97 S. E. 44.

³⁸ Marshall v. Wabash R. Co., 201 Mich. 167, 8 A. L. R. 435, 167 N. W. 19.

³⁹ Estoppel of stockholder who has filed mechanic's lien, to assert priority of his lien over deed of trust, see Feick v. Stephens, 250 Fed. 185.

CHAPTER 35

EXECUTION OF CORPORATE INSTRUMENTS

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I. GENERAL CONSIDERATIONS

§ 1442. **Form and contents—In general.** A signature to estimates of corporate assets of a name of a person followed by the words "Sec'y and Treas. Consolidated Fisheries, Inc." is not the signature of the corporation.¹

§ 1443. — **Affidavits.** Of course corporations may make affidavits through officers and agents.² Where a statute requires the affidavit for publication of summons to be made by the plaintiff, the affidavit may be made by an agent where plaintiff is a corporation.³ What seems to be the carrying of a rule to the extreme limit is a decision in Missouri that a statute authorizing an action against unknown heirs if "any plaintiff shall allege in his petition, under oath," certain things, does not permit such an action by a corporation for the reason that a corporation cannot make an affidavit except by agent or attorney, and the statute requires the affidavit to be made by plaintiff personally.⁴

If a party, as distinguished from his agent or attorney, is required to make an affidavit, then, in case of a corporation, the affidavit must be made by an executive or administrative officer and not by an agent or attorney. The acts of a corporation done through its officers are acts done per se, so far as a corporation may be said to act by itself, while the act of a corporation through a mere agent is an act per alium.⁵

This question is fully annotated in a recent note entitled "Necessity of showing authority or qualification of affiant in affidavit made in behalf of corporation."⁶

§ 1445. **Who may execute.** Although a person signs a contract in the corporate name as "Assistant to the President," his power to sign it is to be determined by the actual office which he holds, so that, for instance, if it is shown he is the

¹ Andrews v. Osius, 203 Mich. 195, 168 N. W. 1032.

² Simmons v. Campbell, — Tex. Civ. App. —, 213 S. W. 338.

³ Jotter v. Charles B. Marvin Inv. Co., — Colo. —, 189 Pac. 22.

⁴ Chilton v. Hedges, — Mo. —, 204 S. W. 900.

⁵ Fidelity & Casualty Co. v. Carroll, 186 Ind. 633, 117 N. E. 858.

⁶ 3 A. L. R. 132, annotating Wakely v. Sun Ins. Office of London, England, 246 Pa. 268, 3 A. L. R. 128, 92 Atl. 136.

general manager, the contract is properly signed if a general manager could do so.⁷

§ 1447. Personal or corporate liability. The word "treasurer" after the name of an officer is descriptio personæ.⁸

§ 1448. Abbreviations. Indorsements for transfer are good without regard to whether the word "company" is spelled out in full or abbreviated "co." or whether the word "secretary" is spelled out or abbreviated "secy." or "sec."⁹

§ 1457. Necessity for approval by certain officers or stockholders. Contracts are approved by the treasurer, as required by their terms, where indorsed "Approved Eastern Advertising Co., by Clinton Elliott, Treas."¹⁰

II. INSTRUMENTS UNDER SEAL

§ 1461. General rules. Where a corporation passes a general resolution or by-law containing building and other restrictions as to the use of property conveyed by it, a covenant in the deed merely binding the grantee in general terms to abide by the by-laws is sufficient.¹¹

§ 1462. Seal as equivalent to signature. A corporate deed must be signed as well as sealed.¹²

§ 1463. Necessity for signature of corporate name. Where a deed in its body purports to be the deed of a corporation and its attesting clause recites that it is signed by the corporation and that its seal is affixed, the deed is that of the corporation rather than of the officer signing it although it is signed only "Owen L. Carr, President."¹³ A deed on its face purporting to be the

⁷ *Raftis v. McCloud River Lumber Co.*, 35 Cal. App. 397, 170 Pac. 176.

⁸ *Dougherty v. Becklenberg*, 205 Ill. App. 491.

⁹ *Santa Marina Co. v. Canadian Bank of Commerce*, 254 Fed. 391.

¹⁰ *Eastern Advertising Co. v. E. L. Patch Co.*, — Mass. —, 127 N. E. 516.

¹¹ *Heyniger v. Levinsohn*, — N. J. L. —, 102 Atl. 631, aff'g (N. J. Ch.), 101 Atl. 189.

¹² *St. Patrick's Religious, Educational & Charitable Ass'n v. Hale*, 227 Mass. 175, 116 N. E. 407.

¹³ *Bickart v. Henry*, — Ind. App. —, 116 N. E. 15.

deed of a corporation and to convey corporate property is effective as such although signed "Geo. S. Cameron, [L. S.] Pres. M. I. Co., Per F. G. Latham. F. G. Latham, Agent." The court said that while a deed executed by an agent must be executed in the name of the principal, yet it is sacrificing substance to form to hold such a deed invalid because not formally executed in the name of the corporation by the officer or agent. The tendency of modern decisions, said the court, "is to ignore the exceedingly technical refinements upon which the rule was established, and give effect to the intention when it is clearly apparent."¹⁴ Where a deed recites that the grantors comprise the last board of directors of a certain corporation but it does not purport to convey the title of that company, and the grantors sign as individuals and not as trustees, the deed conveys merely the title of the individual grantors.¹⁵

§ 1464. Particular officer who must sign. Statutes often require that conveyances of corporate real estate be attested by the secretary of the corporation.¹⁶ The secretary of a corporation is not the "chief executive officer" authorized by statute to sign deeds.¹⁷ Directors may authorize any competent person to execute a mortgage on corporate property notwithstanding a statute providing that any corporation "may" convey lands by deed signed by certain officers, since such a statute is directory and not mandatory.¹⁸

§ 1466. Subscribing witnesses. A stockholder or officer is not incompetent as a witness to a signature of a corporate mortgage or deed.¹⁹

III. SIMPLE CONTRACTS OTHER THAN NEGOTIABLE PAPER

§ 1467. General rules. Where a contract is signed by a corporation by an officer, the fact that he put the wrong title after

¹⁴ *Atlanta & C. A. L. R. Co. v. Limestone-Globe Land Co.*, 109 S. C. 444, 96 S. E. 188.

¹⁵ *Warden v. South Pasadena Realty & Improvement Co.*, 178 Cal. 440, 174 Pac. 26.

¹⁶ *Bentley v. Zelma Oil Co.*, 76 Okla. 116, 184 Pac. 131.

¹⁷ *Douglass v. State Bank*, — Fla. —, 82 So. 593.

¹⁸ *Douglass v. State Bank*, — Fla. —, 82 So. 593.

¹⁹ *Hastey v. Roberts*, 149 Ga. 479, 100 S. E. 569; *Farmers' Bank & Trust Co. v. Fudge*, — S. C. —, 100 S. E. 628.

his name is immaterial where he had power to sign for the corporation.²⁰

§ 1469. Necessity for signature of name of corporation—In general. Where the body of a guaranty clearly shows an intent to bind the corporation, the fact that the signature was merely "Thomas H. Sprinkle, General Agent" does not preclude corporate liability.²¹

§ 1471. Contracts made in name of other person. A corporation may be held liable on a contract entered into by one of its officers in his own name, if it was intended for and inured to the benefit of the corporation, and there is anything on the face of the contract suggesting that it was made for an undisclosed principal.²² Where a corporation is the real lessee and the party for whose benefit the lease was signed by one who signed it in his own name individually, the corporation as well as the signer is liable for the rent.²³

IV. NEGOTIABLE PAPER

§ 1472. General rules. Where a note is signed with the name of a corporation and on the next line "M. D. Gross, Pres.," and on the next line "Tekla Rossmann," the latter is liable individually although he was in fact secretary of the company and intended to sign as such. Parol evidence is not admissible.²⁴ There is no delivery of a note where it was not to be effective until signed by the treasurer in accordance with a by-law requiring his signature.²⁵

§ 1473. Effect of use of word "I" or "We." The use of the expression "I promise to pay" preceding a signature to a note which is the name of both the signing president and of the corporation does not avoid the liability of the corporation, especially

²⁰ Thrailkill v. Crosbyton-South-plains R. Co., 246 Fed. 687, 690, L. R. A. 1918 C 90.

²¹ Willson v. Chicago Bonding & Surety Co., — Mo. —, 214 S. W. 371.

²² Swartz v. Burr, — Cal. App. —, 185 Pac. 411.

²³ McKee's Cash Store v. Otero, 19 Ariz. 418, 171 Pac. 910.

²⁴ Rudolph Wurlitzer Co. v. Rossmann, 196 Mo. App. 78, 190 S. W. 636, decided under Negotiable Instruments Law.

²⁵ In re Continental Engine Co., 234 Fed. 58.

where the corporation has the benefit of the money.²⁶ A note reading "We or either of us promise to pay," in the body of which the "drawers and indorsers severally waive presentment," etc., signed by a corporate name and underneath "George W. Hanna, Pres." is a note of the president as well as that of the corporation.²⁷

§ 1475. Name of corporation not disclosed. Where a note is signed "Tekla Rossmann, Secy.," and the name of no corporation appears either in the body of the note or elsewhere, the signer is liable individually and parol evidence is not admissible to show it was intended to bind the corporation.²⁸

§ 1477. Signature with name of corporation followed by name of officer and title of office. A note signed "Spiller-Beall Co. (L. S.)," and directly below on the next line "R. J. Spiller, Pres.," is the note of the corporation and not a joint note.²⁹ Where a note is signed "The Salina Trust Company, W. B. Middlekauff, L. A. Mergen, Treas.," the latter may show that he signed it merely as a representative of the corporation and that the payee accepted the note as the note of the trust company; the provisions of the Negotiable Instruments Law governing.³⁰

§ 1479. Promise in name of officers as officers. A corporation is not liable on a note signed by its president as a co-maker with a third person, where the money was paid to such third person, without showing that the corporation received a part of the proceeds or that the issuance of the note was authorized by the corporation or that plaintiff had knowledge of any course of dealing which would estop the corporation.³¹

²⁶ Hill Binding Co. v. F. J. Koch Co., 207 Ill. App. 217.

²⁷ Bayh v. Hanna, — Ind. App. —, 122 N. E. 7, recognizing conflict in authorities.

²⁸ Rudolph Wurlitzer Co. v. Rossmann, 196 Mo. App. 78, 190 S. W. 636, decided under Negotiable Instruments Law.

²⁹ Spiller-Beall Co. v. Hirsch, 18 Ga. App. 450, 89 S. E. 587.

³⁰ Solomon Nat. Bank v. Continental Trust Co., — Kan. —, 193 Pac. 316.

³¹ Morris Plan Co. of New York v. Edelman, 164 N. Y. Supp. 166.

V. ACKNOWLEDGMENTS

§ 1487. General considerations. A corporation organized under the laws of Illinois is to be deemed a resident of the state, within the meaning of the chattel mortgage act as to acknowledgments, and the county of its residence is the county in which its principal office is located.³²

§ 1489. Who may take—Stockholder. A notary cannot take an acknowledgment to any instrument in which a corporation in which he owns stock is beneficially interested.³³

§ 1490. — Officer or agent. Secretary of corporation, as notary public, cannot attest a bill of sale to the corporation.³⁴ In New Jersey an acknowledgment of a corporation may be made by an officer executing the instrument outside the state.³⁵

§ 1491. Mode of taking and contents. The form of acknowledgment of corporate mortgages is expressly fixed by statute in some states.³⁶ However, statutory forms of acknowledgments of corporate instruments are often merely permissive.³⁷ Providing that statutory forms of corporate acknowledgment shall be valid is permissive and not mandatory.³⁸ An acknowledgment of a corporate mortgage is bad where it does not state that the acknowledgment is in behalf of the corporation.³⁹ An acknowledgment is insufficient, under the West Virginia statute, where it does not allege that the signing officer signed in behalf of the corporation.⁴⁰ In North Dakota, the certificate of acknowledg-

³² Fairbanks Steam Shovel Co. v. Wills, 240 U. S. 642, 60 L. Ed. 841, aff'g 212 Fed. 688.

³³ In re Ames-Farmer Canning Co., — Iowa —, 179 N. W. 105, applying rule to acknowledgment of agreement submitting a controversy to arbitration.

³⁴ Citizens' Trust Co. v. Butler, — Ga. App. —, 103 S. E. 852.

³⁵ Turner & Seymour Mfg. Co. v. Acme Mfg. Co., — N. J. Eq. —, 110 Atl. 123.

³⁶ J. D. Best & Co. v. Wolf Co., — Colo. —, 185 Pac. 371.

Sufficiency of acknowledgment under North Carolina statutes, see Board of Com'rs v. A. V. Mills & Sons, 236 Fed. 362.

³⁷ P. R. Sinclair Coal Co. v. Missouri-Hydraulic Min. Co., — Mo. App. —, 207 S. W. 266.

³⁸ Turner & Seymour Mfg. Co. v. Acme Mfg. Co., — N. J. Eq. —, 110 Atl. 123.

³⁹ J. D. Best & Co. v. Wolf Co., — Colo. —, 185 Pac. 371.

⁴⁰ Clarksburg Casket Co. v. Valley Undertaking Co., 81 W. Va. 212, 3 A. L. R. 660, 94 S. E. 549.

ment of a corporate mortgage must comply with the statutes, by showing that it was executed by a person authorized to execute it for the corporation; and if defective the record is not notice of the mortgage.⁴¹

The official capacity of the notary was held sufficiently shown where he signed "C. J. Adams, Notary Public, Bibb County, Georgia."⁴²

VI. PAROL EVIDENCE

§ 1492. In general. If one adds to his signature to a contract words indicating that he signs in a representative capacity, parol evidence is admissible to show the intent of the parties.⁴³ At least, this is the rule as between the immediate parties to a bill or note,⁴⁴ especially where governed by the Negotiable Instruments Law.⁴⁵ Thus, where a note is indorsed with the names of several persons with the word "Directors" added, parol evidence is admissible to show whether it was their intention to be bound individually thereby.⁴⁶ If the name of the president and of the corporation is the same, and he signs notes in his name, evidence is admissible to show whether he intended to sign personally or for the corporation.⁴⁷

Parol evidence is also admissible to hold a corporation "upon a contract entered into by its president or manager in his own name, if it was intended for and inured to the benefit of the corporation, and there is anything on the face of the instrument suggesting that it was made for an undisclosed principal."⁴⁸

⁴¹ First Nat. Bank v. Casselton R. & Inv. Co., — N. D. —, 175 N. W. 720.

⁴² Missouri State Life Ins. Co. v. Barnes Const. Co., 147 Ga. 677, 95 S. E. 244.

⁴³ Adams v. Swig, — Mass. —, 125 N. E. 857; Solomon v. New Jersey Indemnity Co., — N. J. L. —, 110 Atl. 813; Salvation Army v. Dorf, 169 N. Y. Supp. 1041; W. C. Dean Jewelry Co. v. Storm, — Okla. —, 166 Pac. 1046; Lummus Cotton Gin Co. v. Cave, 109 S. C. 213, 96 S. E. 64.

⁴⁴ Lexington State Bank v. Rose City Creamery Co., 207 Mich. 81, 173 N. W. 481.

⁴⁵ G. C. Riordan & Co. v. Thornsbury, 178 Ky. 324, 198 S. W. 920; Cooper v. Sonk, 201 Mich. 655, 167 N. W. 842.

⁴⁶ Lexington State Bank v. Rose City Creamery Co., 207 Mich. 81, 173 N. W. 481.

⁴⁷ Hill Binding Co. v. F. J. Koch Co., 207 Ill. App. 217.

⁴⁸ Swartz v. Burr, — Cal. App. —, 185 Pac. 411.

CHAPTER 36

EMINENT DOMAIN

- § 1497. Police power distinguished.
- § 1499. Delegation of right or power—In general.
- § 1500. — Foreign corporations.
- § 1502. Public use—Necessity.
- § 1503. — What constitutes.
- § 1504. Property which may be taken.
- § 1505. What constitutes “taking.”
- § 1506. Compensation.

§ 1497. Police power distinguished. Abolition of grade crossings by statute is an exercise of the police power rather than of the power of eminent domain.¹

§ 1499. Delegation of right or power—In general. The power of eminent domain must be bestowed on a corporation, in order for it to have that power, in express terms or by necessary implication.² Electric railroads have the power of eminent domain where such power is delegated to steam roads, where by statute all steam roads are authorized to use electric power.³ The mere fact that an electric power company is a riparian owner does not give it the power of eminent domain which can be acquired only by legislative grant.⁴ Statutes giving to public utilities the power of eminent domain are to be strictly construed.⁵ A water company may condemn land although it incidentally furnishes a small supply of water outside the municipality.⁶ In Kentucky, by statute, telegraph companies are given power to condemn an easement over a railroad right of way.⁷ In some

¹ *Armour & Co. v. New York*, v. *Hiawassee River Power Co.*, 175 N. H. & H. R. Co., 41 R. I. 361, N. C. 668, 96 S. E. 99.
103 Atl. 1031.

² *Chicago, B. & Q. R. Co. v. Mc-* *Thompson & Nesmith v. Man-*
Cooey, 273 Mo. 29, 200 S. W. 59. *chester Traction, Light & Power*
Co., 78 N. H. 433, 101 Atl. 212.

³ *City of Los Angeles v. Los An-* *Croyle v. Johnstown Water*
geles Pac. Co., 31 Cal. App. 100, Co., 259 Pa. 484, 103 Atl. 303.
159 Pac. 992.

⁴ *Carolina Tennessee Power Co.* *Louisville & N. R. Co. v. West-*
ern U. Tel. Co., 249 Fed. 385.

states, at least, a mining company may condemn a right to use a mining tunnel in common with another mining company.⁸ By statute in some states the statutory right of railroad companies to condemn is based on the condition of inability to make a contract with the owner.⁹

In creating a corporation, the state may impose such conditions as it desires, on the right to exercise the power of eminent domain, and where the corporation accepts the charter it cannot afterwards complain of the conditions.¹⁰

The legislature may grant the power of eminent domain to one public service corporation without granting it to all such corporations or in one or more counties without granting it in all counties.¹¹ Confining the power to condemn to corporations is not unconstitutional as conferring special privileges or immunities.¹²

The public utilities commission may require a public service company to do an act requiring the exercise of eminent domain, under the Illinois statutes, although having no power otherwise to condemn property.¹³ The legislature may delegate to the public service commission the right and duty to compel the exercise of the power of eminent domain by a railroad company to secure the public safety, and this is so although the power of the railroad company to condemn has been exhausted before the order of the public service commission.¹⁴

Consent of the public service commission to joint use of railroad tracks is not a condition precedent to the right of a railroad company to condemn ground for the connecting tracks.¹⁵ Condemnation proceedings by a railroad company cannot be de-

⁸ *Monetaire Min. Co. v. Columbus Rexall Consol. Mines Co.*, — Utah —, 174 Pac. 172.

⁹ *Howard Realty Co. v. Paducah & I. R. Co.*, 182 Ky. 494, 206 S. W. 774.

¹⁰ *Farmers Irrigation Dist. v. Nebraska ex rel. O'Shea*, 244 U. S. 325, 61 L. Ed. 1168, aff'g 98 Neb. 239, L. R. A. 1915 E 687, 152 N. W. 372.

¹¹ *Carolina Tennessee Power Co. v. Hiawassee River Power Co.*, 175 N. C. 668, 96 S. E. 99.

¹² *Sloss-Sheffield Steel & Iron Co. v. O'Rear*, 200 Ala. 291, 76 So. 57.

¹³ *Public Service Co. v. Recktenwald*, 290 Ill. 314, 8 A. L. R. 466, 125 N. E. 271.

¹⁴ *Chicago, B. & Q. R. Co. v. Cavanaugh*, 278 Ill. 609, 116 N. E. 128, approved in *Public Service Co. v. Recktenwald*, 290 Ill. 314, 8 A. L. R. 466, 125 N. E. 271.

¹⁵ *Chicago, M. & St. P. R. Co. v. Franzen*, 287 Ill. 346, 122 N. E. 492.

feated on the ground that no license from the city nor consent of the public utilities commission to construct the track across city streets has been obtained, even if necessary, since that is a matter for subsequent consideration.¹⁶

The Kentucky statute authorizing telegraph companies to condemn easements over the rights of way of railroad companies is to be construed as authorizing condemnation only where some measure or degree of necessity is shown.¹⁷

Where "the legislature has delegated to a corporation the authority to exercise the power of eminent domain, the corporation has also the authority to decide on the necessity for exercising the right, and its decision will be conclusive in the absence of a clear abuse of the right."¹⁸

§ 1500. — Foreign corporations.¹⁹

§ 1502. Public use—Necessity. An ice company is a private as distinguished from a quasi public corporation and has no power of eminent domain.²⁰ The power of eminent domain may be delegated to a company organized to supply the public with gas, electricity, heat and water,²¹ or to a corporation maintaining an electric burglar alarm system.²² A corporation cannot condemn land for the use of a private person.²³ It follows that a railroad which has condemned land for right of way cannot contract with an individual to build a railroad solely for his use on such right of way.²⁴ A railroad company cannot condemn land unless necessary for its operation.²⁵

The right to determine the quantity of land necessary to be taken for public use is largely discretionary with the corpora-

¹⁶ *Pittsburgh, C., C. & St. L. R. Co. v. Gage*, 280 Ill. 639, 117 N. E. 726.

¹⁷ *Louisville & N. R. Co. v. Western U. Tel. Co.*, 249 Fed. 385.

¹⁸ *Chicago, M. & St. P. R. Co. v. Franzen*, 287 Ill. 346, 122 N. E. 492.

¹⁹ See § 5873 et seq., *infra*.

²⁰ *Van Valkenburgh v. Ford*, — Tex. Civ. App. —, 207 S. W. 405.

²¹ *Public Service Co. v. Recktenwald*, 291 Ill. 471, 125 N. E. 271.

²² *Holmes Electric Protective Co. v. Williams*, 228 N. Y. 407, 127 N. E. 315, *rev'g* on other grounds 181 N. Y. App. Div. 687, 168 N. Y. Supp. 746.

²³ *Bradshaw v. Hilton Lumber Co.*, 179 N. C. 501, 103 S. E. 69.

²⁴ *Bradshaw v. Hilton Lumber Co.*, 179 N. C. 501, 103 S. E. 69, following *Stewart's Appeal*, 56 Pa. St. 413.

²⁵ *Houser v. Paducah & I. R. Co.*, 178 Ky. 458, 199 S. W. 3.

tion, and generally the burden is on the landowner to show that the land is to be devoted to a private rather than a public use.²⁶

§ 1503. — What constitutes. A railroad, including its construction, maintenance and operation, is a "public use."²⁷ Condemnation of land by a railroad company for right of way, depots, etc., is for a public use.²⁸ A spur track to be constructed by a railroad partly at its expense to connect with an industrial plant is for a public use.²⁹ Whether a spur track is a "public utility" depends on the right of the public to use it.³⁰ Change of terminal of a railroad and trolley so as to connect detached sections of the campus of Princeton University is a public necessity or use.³¹ Condemnation of water and water rights for the purpose of manufacturing, supplying and selling to the public power produced by water as a motive force, is for a public purpose.³² A water company, in condemning a water supply, may condemn as much water as reasonably necessary not only for present purposes but also for future needs.³³ Taking of water power by an electric railroad company is for a public use although its charter authorizes the sale of surplus power, where the sale of surplus power is not the real object of the condemnation or anything more than a possible incident, necessary to prevent waste, of the primary public use.³⁴ A gas company may condemn land for additional pipe lines although in

²⁶ Pittsburgh & West Virginia Gas Co. v. Cutright, 83 W. Va. 42, 97 S. E. 686.

²⁷ Chicago, B. & Q. R. Co. v. McCoey, 273 Mo. 29, 200 S. W. 59.

²⁸ Howard Realty Co. v. Paducah & I. R. Co., 182 Ky. 494, 206 S. W. 774.

²⁹ Range Sand Lime Brick Co. v. Great Northern R. Co., 137 Minn. 314, L. R. A. 1918 B 784, 163 N. W. 656; Menasha Woodenware Co. v. Railroad Commission, 167 Wis. 19, 166 N. W. 435. See also Southern Pac. Co. v. Los Angeles Milling Co., 177 Cal. 395, 170 Pac. 829.

³⁰ Bradley v. Lithonia & A. M. R. Co., 147 Ga. 22, 92 S. E. 539.

³¹ Rowland v. Mercer County Traction Co., 91 N. J. L. 332, 102 Atl. 814.

³² Mt. Vernon-Woodbury Cotton Duck Co. v. Alabama Interstate Power Co., 240 U. S. 30, 60 L. Ed. 507, aff'g 186 Ala. 622, 65 So. 287, and followed in Hendersonville Light & Power Co. v. Blue Ridge Interurban R. Co., 243 U. S. 563, 61 L. Ed. 900, aff'g 171 N. C. 314, 88 S. E. 245.

³³ Croyle v. Johnstown Water Co., 259 Pa. 484, 103 Atl. 303.

³⁴ Hendersonville Light & Power Co. v. Blue Ridge Interurban R. Co., 243 U. S. 563, 61 L. Ed. 900, aff'g 171 N. C. 314, 88 S. E. 245.

part to make gasoline for private purposes, where the extraction of such gasoline betters the quality of the gas and improves the service.³⁵ The use of water for irrigation purposes constitutes a public use,³⁶ although in California it is held that irrigation is not a "public use" within the eminent domain law.³⁷ In any event, an irrigation company cannot condemn land for a canal where the water is to be devoted solely to the irrigation of its own lands, since not for a "public use."³⁸ The Utah statutes in effect declare mining generally and the development of mines a public use.³⁹ A temporary steam tramway, laid down in a city street by a contracting company for hauling dump cars from the excavation in building the New York City subway, was not a "public use" of the street.⁴⁰

§ 1504. Property which may be taken. Power to condemn real property includes only what is reasonably necessary.⁴¹ The power of a quasi public corporation to condemn property owned by a municipality does not exist unless clearly created by statute.⁴² A coal company cannot, in Utah, condemn any portion of a railroad right of way for a tippie site.⁴³ Statutory authority to condemn for "docks" includes a waterway.⁴⁴ Parts of an interstate railroad right of way and of bridges over navigable waters may be condemned for the use of a telegraph company pursuant to a state law.⁴⁵ A power company may condemn water rights although it amounts to the taking away of the

³⁵ *Pittsburgh & West Virginia Gas Co. v. Cutright*, 83 W. Va. 42, 97 S. E. 686.

³⁶ *Young v. Dugger*, 23 N. M. 613, 170 Pac. 61.

³⁷ *Gravelly Ford Canal Co. v. Pope & Talbot Land Co.*, — Cal. App. —, 178 Pac. 150.

³⁸ *Gravelly Ford Canal Co. v. Pope & Talbot Land Co.*, — Cal. App. —, 178 Pac. 150.

³⁹ *Monetaire Min. Co. v. Columbus Rexall Consol. Mines Co.*, — Utah —, 174 Pac. 172.

⁴⁰ *Bradley v. Degnon Contracting Co.*, 224 N. Y. 60, 120 N. E. 89, aff'g 179 N. Y. App. Div. 916, 165 N. Y. Supp. 1078.

⁴¹ *St. Louis & S. F. R. Co. v. Mann*, — Okla. —, 192 Pac. 231, citing 2 *Fletcher Cye. Corp.* § 1086.

⁴² *State ex rel. City of Cle Elum v. Kittitas County*, 107 Wash. 326, 181 Pac. 698.

⁴³ *Ketchum Coal Co. v. Pleasant Valley Coal Co.*, 50 Utah 395, 168 Pac. 86.

⁴⁴ *State ex rel. Patterson v. Superior Court for King County*, 102 Wash. 331, 173 Pac. 186.

⁴⁵ *Louisville & N. R. Co. v. Western U. Tel. Co.*, 250 U. S. 363, 63 L. Ed. 1032, aff'g 233 Fed. 82 and 107 Miss. 626, 65 So. 650.

right of a lumber company as riparian owner to float its logs, where required by the public interest.⁴⁶ The fact that a power company intends to appropriate water power to a public use at some future time, where such intent is not unmistakably evidenced by conduct which practically guarantees its speedy consummation, does not bar proceedings by a city to condemn rights in a stream acquired by the power company.⁴⁷

Corporate property may be condemned by a municipality, including a franchise.⁴⁸

§ 1505. What constitutes "taking."⁴⁹ The establishment of a municipal street railway system does not constitute a taking of the property of a street railway owned by a private corporation whose franchise does not prohibit such a rival.⁵⁰ The construction of a steam railroad upon a street or highway, the fee of which is owned by abutting owners, constitutes a "taking" of the property.⁵¹ Changing the location of a railroad is not a taking, injury to, or destruction of the rights of landowners.⁵² A corporation purchasing the property and assets of another, and by user continuing a consequential injury to other land, is liable for damages although the original wrongful appropriation of land was by the selling corporation.⁵³

§ 1506. Compensation.⁵⁴ Statutory scheme for condemnation of property by public corporations by a proceeding wherein

⁴⁶ *State ex rel. South Fork Driving Co. v. Superior Court for Pacific County*, 102 Wash. 460, 173 Pac. 192.

⁴⁷ *East Hartford Fire Dist. v. Glastonbury Power Co.*, 92 Conn. 217, 102 Atl. 592.

⁴⁸ *State ex rel. Bruenting Realty Co. v. Thomas*, 278 Mo. 85, 211 S. W. 667.

⁴⁹ Sufficiency of notice of condemnation proceedings by a railroad company, see *Central of Georgia R. Co. v. Bibb Brick Co.*, 149 Ga. 38, 99 S. E. 126.

⁵⁰ *United Railroads of San Francisco v. City & County of San Francisco*, 249 U. S. 517, 63 L. Ed. 739.

⁵¹ *City of Orange v. Rector*, — Tex. Civ. App. —, 205 S. W. 503.

⁵² *Bryan v. Louisville & N. R. Co.*, 244 Fed. 650.

⁵³ *Hazard Dean Coal Co. v. McDutosh*, 183 Ky. 316, 209 S. W. 364.

⁵⁴ Damages in case of condemnation by telegraph company of easement over a railroad right of way, see *Louisville & N. R. Co. v. Western U. Tel. Co.*, 249 Fed. 385.

Note on "Building restriction or restrictive agreement as binding public or public service corporation," see *Ann. Cas.* 1918 B 591.

the value is to be fixed by the public service commission, and the power to condemn by the courts, is constitutional.⁵⁵ Increased transportation facilities are not direct benefits to the land not taken which may be set off in condemnation proceedings by a railroad company.⁵⁶

⁵⁵ Marin Municipal Water Dist. v. Marin Water & Power Co., 178 Cal. 308, 173 Pac. 469.

⁵⁶ Tyson Creek R. Co. v. Empire Mill Co., 31 Idaho 580, 174 Pac. 1004.

CHAPTER 37

ULTRA VIRES

I. GENERAL CONSIDERATIONS

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- § 1511. Definition—Strict construction.
- § 1512. — Distinguished from acts expressly prohibited or against public policy.
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VIII. OBLIGATION TO RESTORE BENEFITS RECEIVED UNDER ULTRA VIRES CONTRACT: REMEDIES OF PARTIES TO ULTRA VIRES CONTRACT OTHER THAN ACTION ON CONTRACT ITSELF

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§ 1604. Action on implied contract—In general.

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I. GENERAL CONSIDERATIONS

§ 1507. Introductory.¹

§ 1511. Definition—Strict construction. The term “ultra vires” may indicate (1) that the act referred to is entirely beyond the scope of the powers of the corporation to perform under any circumstances or for any purpose or (2) that the act is one within the scope of the general powers of the corporation for some purposes but beyond such powers for other purposes.² In Alabama, it is said that an ultra vires contract

¹For article on ultra vires, its nature, elements and modern application, see 54 Am. L. Rev. 535-562.

There is an extended note on “Ultra Vires in Actions on Corporate Contracts” in 36 Dom. L. Rep. (Can.) 107-151.

Doctrine of ultra vires in rela-

tion to incorporated companies in Canada, see 40 Canadian L. T. 993-1007.

Ultra vires corporate acts under the California decisions, see article in 6 Cal. L. Rev. 319-330.

²James Eva Estate v. Mecca Co., — Cal. App. —, 181 Pac. 415.

is "one that is wholly and manifestly outside of the charter or constituent act of the corporation or some valid legislative act applicable to it."³ In Kentucky, it is held that ultra vires contracts include not only those entirely without the scope and purpose of the charter and not pertaining to the objects for which the corporation was chartered, but also those "beyond the limitations of the powers conferred by the charter although within the purposes contemplated by the articles of incorporation."⁴ In Texas, after stating the different senses in which the term "ultra vires" is used, it is said that "accurately, the term 'ultra vires' applies only to those acts which are wholly beyond the power of the corporation—acts which it has not the power to perform under any circumstances."⁵

§ 1512. — Distinguished from acts expressly prohibited or against public policy. Acts merely ultra vires are distinguishable from acts expressly prohibited,⁶ although in one case it was said that "contracts that are illegal are certainly ultra vires."⁷

§ 1516. Ultra vires acts as the acts of the corporation. A corporation may perform ultra vires acts until restrained by a stockholder or by the state under a writ of quo warranto.⁸

§ 1517. Estoppel to deny power to contract. There is no estoppel to resist an ultra vires contract merely because of the making of the contract.⁹ However, there may be an estoppel of a corporation, by its acts, to plead ultra vires, provided the contract is not one expressly forbidden by statute.¹⁰ "Estoppel" to plead ultra vires seems, according to some judges, to be confined to cases "where an act was within the power

³ Alabama City, G. & A. R. Co. v. Kyle, 202 Ala. 552, 81 So. 54.

⁴ American Southern Nat. Bank v. Smith, 170 Ky. 512, Ann. Cas. 1918 B 959, 186 S. W. 482.

⁵ Taylor Feed Pen Co. v. Taylor Nat. Bank, — Tex. —, 215 S. W. 850.

⁶ Richardson v. Bermuda Land & Live Stock Co., — Tex. Civ. App. —, 210 S. W. 746.

⁷ Eckhart v. Heier, 38 S. D. 524, 162 N. W. 150.

⁸ Clark v. Groger, 102 Wash. 188, 172 Pac. 1164.

⁹ Alabama Red Cedar Co. v. Tennessee Valley Bank, 200 Ala. 622, 76 So. 980.

¹⁰ Denecke v. West, 184 Iowa 600, 169 N. W. 97.

of the corporation for some purposes or under some circumstances, and in which one dealing with it in good faith could assume the existence of the conditions warranting the act.”¹¹ Where an estoppel to set up ultra vires is claimed, it seems that all the elements of an estoppel in pais must concur.¹² Where the other party to the contract has not been misled, it cannot set up that the corporation is estopped to urge ultra vires.¹³ There is no estoppel to plead ultra vires merely because as a result of the ultra vires contract money was received by a director assuming to act for the corporation where he never turned the money over to the corporation nor applied it to any corporate purpose.¹⁴

§ 1518. Ratification. Ultra vires acts cannot be ratified so as to validate them,¹⁵ except by the legislature. Ultra vires debts may be rendered legal by the legislature, by subsequent statutes, without interference with vested rights of stockholders or violating due process of law or exercising a judicial function.¹⁶

Where creditors are all paid, and all the stockholders consent, a corporation may become an accommodation indorser.¹⁷ Stockholders, by ratification of an act, waive the right to themselves urge that it is ultra vires.¹⁸

§ 1520. Defense not favored. The doctrine of ultra vires, whether invoked for or against a corporation, is not favored in the law.¹⁹ “The defense,” it has been said, “must always

¹¹ Taylor Feed Pen Co. v. Taylor Nat. Bank, — Tex. —, 215 S. W. 850.

¹² Taylor Feed Pen Co. v. Taylor Nat. Bank, — Tex. —, 215 S. W. 850.

¹³ Taylor Feed Pen Co. v. Taylor Nat. Bank, — Tex. —, 215 S. W. 850.

¹⁴ Taylor Feed Pen Co. v. Taylor Nat. Bank, — Tex. —, 215 S. W. 850.

¹⁵ National Trust & Credit Co. v. F. H. Orcutt & Son Co., 259 Fed. 830; Mobile Elec. Co. v. City of Mobile, 201 Ala. 607, 79 So. 39;

Alabama Red Cedar Co. v. Tennessee Valley Bank, 200 Ala. 622, 76 So. 980; United Vacuum Sweeper Co. v. Groth, 210 Ill. App. 358.

¹⁶ Brown v. Boston & M. Ry., 233 Mass. 428, 124 N. E. 322.

¹⁷ Sargent v. Palace Café Co., 175 Cal. 737, 167 Pac. 146.

¹⁸ Lumbermen's Trust Co. v. Title Ins. & Inv. Co., 248 Fed. 212, 221.

¹⁹ Thrailkill v. Crosbyton-South Plains R. Co., 246 Fed. 687, 691, L. R. A. 1918 C 90.

be considered on the merits in law and fact," without following any procrustean rule.²⁰ The defense of ultra vires "should never be sustained where it will defeat the ends of justice, where such a result can be avoided."²¹ A "court of equity never allows a corporation to obtain an unconscionable advantage by pleading that its own contracts were ultra vires."²² Public policy may demand that a corporation shall not escape liability by setting up ultra vires.²³

The attempt of a corporation to use the defense of ultra vires as a means of escaping its liability to third persons is regarded with much less favor than when a direct attack upon such corporate act is made by a stockholder or by the state.²⁴

In support of what is stated in the text in volume 3 in regard to this matter, attention is called to this statement by Chief Justice Ostrander of the Michigan Supreme Court: "If the court could weigh one resulting injustice against another, it could not enforce this demand except by doing injustice to some, although a minority, of the unoffending shareholders of defendant."²⁵

§ 1521. Contracts ultra vires in part only. That part of a contract is ultra vires does not necessarily vitiate the entire contract;²⁶ and hence liability cannot be avoided on an intra vires contract by asserting an ultra vires agreement connected therewith.²⁷ Where a contract is severable, the fact that part of it is ultra vires does not vitiate the valid part.²⁸ Where a contract and bond are one and indivisible, and the contract is ultra vires, the bond is invalid.²⁹

²⁰ United States Fidelity & Guaranty Co. v. Cascade Const. Co., 106 Wash. 478, 180 Pac. 463.

²¹ United States Fidelity & Guaranty Co. v. Cascade Const. Co., 106 Wash. 478, 180 Pac. 463.

²² In re Litchfield County Agr. Society, 91 Conn. 536, 100 Atl. 356.

²³ United States Fidelity & Guaranty Co. v. Cascade Const. Co., 106 Wash. 478, 180 Pac. 463.

²⁴ James Eva Estate v. Mecca Co., — Cal. App. —, 181 Pac. 415.

²⁵ Stone-Ordean-Wells Co. v. New

England Pie Co., 201 Mich. 407, 167 N. W. 943.

²⁶ Fogarty v. Hunter, 83 Ore. 183, 162 Pac. 964.

²⁷ Wegner v. First Nat. Bank, — N. D. —, 173 N. W. 814.

²⁸ Fogarty v. Hunter, 83 Ore. 183, 162 Pac. 964; Rousseau v. Everett, — Tex. Civ. App. —, 209 S. W. 460.

²⁹ American Credit & Trust Co. v. New Era Chandelier Co., 208 Ill. App. 181.

Sureties on bonds to a corporate obligee are liable even though the transaction may be ultra vires to the corporation, but it is otherwise where the bond is not merely ultra vires but is illegal.³⁰

II. WHO MAY URGE ULTRA VIRES

§ 1523. In general. The other party to a contract with a corporation cannot be relieved therefrom on the ground that it is ultra vires.³¹ A receiver, in resisting the allowance of a claim filed against the insolvent corporation, may interpose any defense which the corporation itself could have interposed, including the defense of ultra vires.³²

§ 1524. State—General rules. Ultra vires acts may be enjoined by the public service commission, in a proper case.³³

§ 1526. Stockholders. Stockholders who consent to an act cannot attack it as ultra vires.³⁴ Stockholders who are officers of the corporation and practically the corporation itself cannot question the power of the corporation to do acts performed by themselves.³⁵ The attorney general is the only one who can attack the issuance of a new class of preferred stock as ultra vires. The issuance will not be enjoined at the suit of a professional agitator who purchased a small amount of stock to prevent such issuance.³⁶

§ 1527. Strangers—General rules. A stranger not a party to a contract cannot interpose the plea of ultra vires,³⁷ unless

³⁰ *Zurn v. Mitchell*, — Tex. Civ. App. —, 196 S. W. 544.

³¹ *City of Belfast v. Belfast Water Co.*, 115 Me. 234, L. R. A. 1917 B 908, 98 Atl. 73.

³² A receiver sued on a claim may set up ultra vires at least where the corporation has not received any benefits in connection with its lawful business. *Wiley Fertilizer Co. v. Carroll*, 202 Ala. 335, 80 So. 417.

³³ *Public Service Commission v.*

J. & J. Rogers Co., 103 N. Y. Misc. 711, 170 N. Y. Supp. 964.

³⁴ *Baillie v. Columbia Gold Min. Co.*, 86 Ore. 1, 167 Pac. 1167; *Hoberg v. John Hoberg Co.*, 170 Wis. 50, 173 N. W. 639, 952.

³⁵ *Welden v. Stephens Farm Loan Co.*, — Mo. —, 213 S. W. 54.

³⁶ *General Inv. Co. v. Bethlehem Steel Corporation*, 88 N. J. Eq. 237, 102 Atl. 252.

³⁷ *Gigoux v. Moore*, 105 Kan. 361, 184 Pac. 637; *Diggs v. Morgan Col-*

the ultra vires act is a public nuisance.³⁸ Thus, where a corporation which was an accommodation indorser paid the note and sued a prior indorser, the latter could not defend on the ground that the accommodation indorsement was ultra vires.³⁹ So a private citizen cannot enjoin an incorporated club from selling liquor on the theory that it is ultra vires.⁴⁰ In ejectment between third persons, the power of a corporation to hold or dispose of property cannot be attacked.⁴¹ Property owners who seek to enjoin a corporation from erecting a hotel on land claimed to have been dedicated to the public cannot raise the question that the erection of the hotel is ultra vires.⁴² An adjoining landowner cannot enjoin a corporation from exceeding its powers by using part of its property to establish a residential negro colony, where not amounting to a public nuisance.⁴³ The objection that a conveyance of its plant by a construction company to its surety was ultra vires cannot be urged by one who had given a mortgage to the surety as indemnity, but only by the corporation.⁴⁴

§ 1529. — Creditors. Creditors cannot assail a merely ultra vires act unless it also results in depleting the assets of the corporation in fraud of creditors.⁴⁵ In any event, subsequent creditors ordinarily cannot attack acts as ultra vires.⁴⁶

III. CONTRACTS EXECUTORY ON BOTH SIDES

§ 1530. General rule. A corporation cannot sue for damages for breach of contract where it had no charter power to make the

lege, 133 Md. 264, 105 Atl. 157;
Norment v. First Nat. Bank, 23
N. M. 198, 167 Pac. 731.

A stranger cannot, by mandamus, question the action of a corporation as ultra vires. Clements v. Williams, 191 N. Y. App. Div. 279, 181 N. Y. Supp. 230.

³⁸ Diggs v. Morgan College, 133 Md. 264, 105 Atl. 157.

³⁹ Hazelwood Brewing Co. v. Siebert, 256 Pa. 9, 100 Atl. 493.

⁴⁰ Rowan v. Stowe, — Tex. Civ. App. —, 193 S. W. 434.

⁴¹ Daniel v. Wade, — Ala. —, 83 So. 99.

⁴² Weihe v. Macatawa Resort Co., 198 Mich. 334, 164 N. W. 510.

⁴³ Diggs v. Morgan College, 133 Md. 264, 105 Atl. 157.

⁴⁴ Angle v. Bankers' Surety Co., 244 Fed. 401.

⁴⁵ Brent v. Simpson, 238 Fed. 285, 291. See also Hilgers v. Goselin, 190 N. Y. App. Div. 346, 179 N. Y. Supp. 703.

⁴⁶ Gulf Pipe Line Co. v. Lasater, — Tex. Civ. App. —, 193 S. W. 773.

contract.⁴⁷ Ultra vires is a defense, in California, where a national bank is sought to be held liable for damages for its failure to lend money for another, as broker, on sound security.⁴⁸

§ 1531. Specific performance.⁴⁹

IV. CONTRACTS EXECUTED ON ONE SIDE ONLY

§ 1538. State courts as bound to follow federal courts and vice versa. Federal courts must follow state decisions as to the effect of ultra vires.⁵⁰

§ 1539. Rule of federal courts and some state courts—In general. "In the United States courts, it is settled that part performance will not save an ultra vires contract, and that no amount of performance of an ultra vires contract, even for a long period, or the receipt by the corporation raising the question of the consideration for such a contract, operates to estop the corporation from challenging the validity of the contract or refusing further to perform."⁵¹

§ 1541. — State courts which follow federal rule.⁵² Included in this class, among others, are the courts of Alabama⁵³ and Tennessee.⁵⁴

⁴⁷ Jones v. Mississippi Farms Co., 116 Miss. 295, 76 So. 880.

⁴⁸ Pollock v. Lumbermen's Nat. Bank, 83 Ore. 324, 168 Pac. 616.

⁴⁹ That a corporation cannot enforce an ultra vires contract by specific performance, see Jones v. Mississippi Farms Co., 116 Miss. 295, 76 So. 880.

⁵⁰ Graysonia-Nashville Lumber Co. v. Goldman, 247 Fed. 423.

⁵¹ Bassick v. Aetna Explosives Co., 246 Fed. 974, 1004. Contra, see Clinchfield Fuel Co. v. Henderson Iron Works Co., 254 Fed. 411.

⁵² Illinois rule, see United Vacuum Sweeper Co. v. Groth, 210 Ill. App. 358.

Rule in Missouri, see Orpheum

Theater & Realty Co. v. Seavey & Flarsheim Brokerage Co., 197 Mo. App. 661, 199 S. W. 257.

⁵³ Paterson & Edey Lumber Co. v. Bank of Mobile, — Ala. —, 84 So. 721; Wiley Fertilizer Co. v. Carroll, 202 Ala. 335, 80 So. 417.

In Alabama "there can be no estoppel to resist a contract beyond the power of the corporation, and no ratification of such a contract." Alabama Red Cedar Co. v. Tennessee Valley Bank, 200 Ala. 622, 76 So. 980.

⁵⁴ Dillard & Coffin Co. v. Richmond Cotton Oil Co., 140 Tenn. 290, 204 S. W. 758, holding, however, that benefits may be recovered back.

§ 1543. **Majority rule in state courts—In general.** Under this rule, ultra vires cannot be pleaded by a corporation sued to recover damages for breach of an ultra vires contract.⁵⁵

§ 1546. — **Necessity for receipt of benefits.** Ultra vires ordinarily is a defense where the corporation has received no benefits and no injustice will arise from its allowance.⁵⁶ For instance, a corporation is not estopped to set up ultra vires as a defense to an action against it on a guaranty beyond its powers where it has not received any benefit therefrom.⁵⁷ So an ultra vires agreement of a bank, in making a loan, to accept a share of the profits of the borrower as payment, where the bank in fact received nothing, does not estop the bank to set up ultra vires.⁵⁸ It must appear that the corporation, in the operation of its franchise rights and powers, received the benefits in the line of its necessary business and operation.⁵⁹ Benefits to stockholders as individual owners of land is not a benefit to the corporation such as to prevent it from pleading ultra vires.⁶⁰

§ 1547. — **States in which rule prevails.** The rule that a corporation cannot invoke the doctrine of ultra vires where it

⁵⁵ Donaldsonville Live Stock Co. v. Corporation Service Co., — Ga. App. —, 100 S. E. 731.

⁵⁶ First Nat. Bank v. Stokes, 134 Ark. 368, 203 S. W. 1026; Orpheum Theater & Realty Co. v. Seavey & Flarsheim Brokerage Co., 197 Mo. App. 661, 199 S. W. 257; Kaplan Dry Goods Co. v. Sanger Bros., — Tex. Civ. App. —, 214 S. W. 485.

It was contended in Washington that “only in cases where the defending corporation receives actual benefit has this court ever refused to sustain a defense of ultra vires”; but the court cited Creditors’ Claim & Adjustment Co. v. Northwest Loan & Trust Co., 81 Wash. 247, L. R. A. 1917 A 737, Ann. Cas. 1916 D 551, 142 Pac. 670, as an illustration of a case where no benefit was actually received by

the defending corporation, and held that where a corporation can save itself from ultimate loss on an ultra vires contract of indemnity, it would defeat the ends of justice to allow it to set up the defense of ultra vires. United States Fidelity & Guaranty Co. v. Cascade Const. Co., 106 Wash. 478, 180 Pac. 463.

⁵⁷ Stone-Ordean-Wells Co. v. New England Pie Co., 201 Mich. 407, 167 N. W. 943.

⁵⁸ In re Machine Metal Products Co., 251 Fed. 280.

⁵⁹ Richardson v. Bermuda Land & Live Stock Co., — Tex. Civ. App. —, 210 S. W. 746.

⁶⁰ Orpheum Theater & Realty Co. v. Seavey & Flarsheim Brokerage Co., 197 Mo. App. 661, 199 S. W. 257.

has accepted the benefits of the alleged ultra vires contract prevails, among other states, in Arkansas,⁶¹ Florida,⁶² Georgia,⁶³ Iowa,⁶⁴ Kansas,⁶⁵ New York,⁶⁶ Oklahoma,⁶⁷ Oregon,⁶⁸ Pennsylvania,⁶⁹ Washington,⁷⁰ and West Virginia.⁷¹ In Texas, most of the decisions follow the majority rule,⁷² although in some decisions the rule is modified by laying down the rule that if the act is one which the corporation has no power to do under any circumstances, ultra vires is a defense regardless of benefits received; but if the act is one within the general powers but not authorized in the particular case the act is not ultra vires in the strict and proper sense and ultra vires is no defense.⁷³

⁶¹ In Arkansas, "one who has received the benefit of a contract which is simply ultra vires and not contrary to good morals may not plead the defense of ultra vires." *Graysonia-Nashville Lumber Co. v. Goldman*, 247 Fed. 423, 428.

⁶² *Grand Lodge Knights of Pythias v. State Bank*, — Fla. —, 84 So. 528.

⁶³ *Donaldsonville Live Stock Co. v. Corporation Service Co.*, — Ga. App. —, 100 S. E. 731.

⁶⁴ *Wright v. Johnston*, 183 Iowa 807, 167 N. W. 680.

⁶⁵ *Kelly v. Central Union Fire Ins. Co.*, 101 Kan. 91, L. R. A. 1918 C 1170, 165 Pac. 806; *First Nat. Bank of Eureka v. Wilson*, 101 Kan. 72, 165 Pac. 859; *Saylors v. State Bank of Allen*, 99 Kan. 515, 163 Pac. 454.

A bank cannot escape liability as bailee for a special deposit of securities by the plea of ultra vires. *Security Nat. Bank v. Home Nat. Bank*, 106 Kan. 303, 187 Pac. 697.

⁶⁶ *Higgins v. Hocking Valley R. Co.*, 188 N. Y. App. Div. 684, 177 N. Y. Supp. 444.

This rule "should not be extended so as to protect the corporation's directors upon contracts authorized by themselves that es-

tablish, not only illegality, but such a breach of fiduciary obligations as amounts to bad faith." *Palmer v. Scheftel*, 183 N. Y. App. Div. 77, 170 N. Y. Supp. 588.

⁶⁷ *Bennett v. W. A. Gage & Co.*, — Okla. —, 176 Pac. 744; *Southwestern Surety Ins. Co. v. Davis*, 53 Okla. 332, 156 Pac. 213.

⁶⁸ *National Sales Co. v. Manciet*, 83 Ore. 34, L. R. A. 1917 D 485, 162 Pac. 1055.

⁶⁹ *Lemmon v. East Palestine Rubber Co.*, 260 Pa. 28, 103 Atl. 510.

⁷⁰ *Flanagan v. American Minerals Producing Co.*, 108 Wash. 569, 185 Pac. 609.

⁷¹ *Chafin v. Main Island Creek Coal Co.*, — W. Va. —, 102 S. E. 291.

⁷² *First Nat. Bank v. Crespi & Co.*, — Tex. Civ. App. —, 217 S. W. 705; *Eddleman v. Wofford*, — Tex. Civ. App. —, 217 S. W. 221; *Hollis Cotton Oil, Light & Ice Co. v. Marrs & Lake*, — Tex. Civ. App. —, 207 S. W. 367; *Bay City Bank & Trust Co. v. Rice-Stix Dry Goods Co.*, — Tex. Civ. App. —, 195 S. W. 344. See also *Kaplan Dry Goods Co. v. Sanger Bros.*, — Tex. Civ. App. —, 214 S. W. 485.

⁷³ *Taylor Feed Pen Co. v. Taylor*

The rule in Canada is the same as the majority rule in the United States.⁷⁴

§ 1548. — Application of rule to sales or services rendered.

A corporation which has received the benefit of services rendered cannot set up *ultra vires* as a defense when sued for the amount due.⁷⁵

§ 1549. — Application of rule to loans by corporation. *Ultra vires* is no defense to a corporate agreement to repay money received by the corporation.⁷⁶ Only the United States can set up the want of power of a national bank to loan money on real estate security.⁷⁷

§ 1550. — Application of rule to borrowing of money by corporation. Want of power to borrow money is no defense to a bank where it has received the benefit of the loan.⁷⁸

§ 1557. — Application of rule to contract of guaranty or suretyship. A corporation cannot defend an action on a guaranty on the ground of *ultra vires* where it has received the benefit of the contract.⁷⁹ A company which guaranteed the bonds of a subsidiary company, and received all the benefits from the sale of such bonds, is estopped to plead that its guaranty was *ultra vires*.⁸⁰ *Ultra vires* is no defense to a bank when sued on a guaranty which the person guaranteed has relied on to his detriment.⁸¹

Nat. Bank, — Tex. —, 215 S. W. 850.

⁷⁴ *In re Colonial Assurance Co.*, 34 Dom. L. Rep. (Can.) 341.

⁷⁵ *Flanagan v. American Minerals Producing Co.*, 108 Wash. 569, 185 Pac. 609.

⁷⁶ *Eddleman v. Wofford*, — Tex. Civ. App. —, 217 S. W. 221.

⁷⁷ *Perkins v. First Nat. Bank*, 18 Ga. App. 564, 90 S. E. 91.

⁷⁸ *Farmers' State Bank v. Couture*, — N. D. —, 178 N. W. 138.

⁷⁹ *United States Industrial Alcohol Co. v. Distilling Co.*, 87 N. J. Eq. 531, 104 Atl. 216, aff'g 100

Atl. 620; *Lemmon v. East Palestine Rubber Co.*, 260 Pa. 28, 103 Atl. 510.

That a guaranty by a corporation was *ultra vires* is no defense to an action on it where the agreement has been fully carried out by the party to protect whom the guaranty was given to the benefit of the corporation. *Standard Brewery v. Creedon*, 283 Ill. 474, 119 N. E. 581, aff'g 204 Ill. App. 431.

⁸⁰ *Higgins v. Hocking Valley R. Co.*, 188 N. Y. App. Div. 684, 177 N. Y. Supp. 444.

⁸¹ *El Paso Bank & Trust Co. v.*

V. CONTRACTS FULLY EXECUTED ON BOTH SIDES

§ 1559. General rules. Executed ultra vires contracts can be attacked only by the state.⁸² Where title is acquired by ultra vires acts, the fact of ultra vires does not reinvest the seller with the title nor vest it in another.⁸³

§ 1561. Application of rule to conveyances of "real" property "to" corporation—In general.⁸⁴ If the acquisition and holding of land is ultra vires, no one but the state can complain.⁸⁵ If a corporation is not authorized to acquire real estate except in a limited amount for prescribed purposes, the acquisition of additional property cannot be questioned by a private individual but only by the state.⁸⁶ An individual in litigation with a corporation cannot take advantage of the fact that the company has not complied with the provisions of the statute with reference to holding real property.⁸⁷

The rule that the power of a corporation to own land at all, or in excess of the amount or kind prescribed by its charter, cannot be questioned collaterally but only in a direct proceeding instituted by the state for that purpose, does not apply where the corporation is seeking in court to acquire lands which it has no power to acquire and hold.⁸⁸

First State Bank, — Tex. Civ. App. —, 202 S. W. 522.

Ultra vires is no defense as against a guaranty by a corporation where it has been relied on and goods furnished by the other party in pursuance thereof. *Hoosier Brick Co. v. Floyd County Bank*, 64 Ind. App. 445, 116 N. E. 87.

⁸² *Spadra-Clarksville Coal Co. v. Security Nat. Bank*, — Tex. Civ. App. —, 206 S. W. 200.

⁸³ *Spadra-Clarksville Coal Co. v. Security Nat. Bank*, — Tex. Civ. App. —, 206 S. W. 200.

⁸⁴ Article on whether capacity of a corporation to take a conveyance of real estate can be called in

question in a collateral way by any one other than the state, see 84 Cent. L. J. 174-180.

⁸⁵ *McCann v. Children's Home Society*, 176 Cal. 359, 168 Pac. 355; *Hight v. Richmond Park Imp. Co.*, 47 App. Cas. (D. C.) 518, 533; *Cross v. Seaboard Air Line R. Co.*, 172 N. C. 119, 90 S. E. 14; *Coal Land Development Co. v. Chidester*, — W. Va. —, 103 S. E. 923.

⁸⁶ *Union Trust Co. v. Hendrickson*, — Okla. —, 172 Pac. 440.

⁸⁷ *Reichert v. Ellis Ferry Co.*, 184 Ky. 150, 211 S. W. 403.

⁸⁸ *Southern Realty Co. v. Tchula Co-Operative Stores*, 114 Miss. 309, 75 So. 121.

§ 1565. — **Statutory prohibitions.** The constitutional provision prohibiting corporations from acquiring real estate not for use in the business, with certain exceptions, is not self-executing, and a violation thereof does not cause an escheat of the property to the state.⁸⁹

§ 1568. — **Right of parties to transfer to attack.** Violation of its articles of incorporation cannot be set up by defendant in an action by the corporation to recover land.⁹⁰ Even where land is acquired in violation of an express statute, title is vested in the corporation and such unlawful acquisition of the title can only be questioned by the state, through its proper officers, and not by the grantor in the deed of trust under which the corporation purchased at foreclosure sale.⁹¹

§ 1574. **Application of rule to ultra vires conveyance or transfer "by" corporation—General rule.** Where a corporation is the vendor, the vendee cannot set up its want of capacity to take and hold land as a defense to an action to recover the purchase price of land sold to him.⁹² The power of a corporation to sell real estate for profit cannot be questioned collaterally but only by a direct proceeding by the state.⁹³

§ 1581. **Devise or bequest—In general.** Only the state can attack a gift to a foreign religious corporation as in violation of the public policy of the state.⁹⁴

VII. CONTRACTS APPARENTLY WITHIN POWERS OF CORPORATION

§ 1591. **Introductory.** It is presumed that a power conferred on a corporation, when exercised, is exercised legally and not in violation of the law.⁹⁵

⁸⁹ Parwal Inv. Co. v. State, — Okla. —, 175 Pac. 514.

⁹⁰ Troy & North Carolina Gold Min. Co. v. Snow Lumber Co., 173 N. C. 593, L. R. A. 1917 E 892, 92 S. E. 494.

⁹¹ Middleton v. Georgetown Mercantile Co., 117 Miss. 134, 77 So. 956.

⁹² Westbrook v. Missouri-Texas

Land & Irrigation Co., — Tex. Civ. App. —, 195 S. W. 1154.

⁹³ Coal Land Development Co. v. Chidester, — W. Va. —, 103 S. E. 923.

⁹⁴ Stump v. Sturm, 254 Fed. 535.

⁹⁵ United States Industrial Alcohol Co. v. Distilling Co., 87 N. J. Eq. 531, 104 Atl. 216, aff'g (N. J. Ch.), 100 Atl. 620.

§ 1592. Whether included within term ultra vires.⁹⁶

§ 1593. Statement of rule. Where a corporate act is not merely an abuse or excess of power but is wholly beyond its powers, it is void and its illegality may be urged by any party affected by it.⁹⁷ The California rule is that where an act is within the power of the corporation for some purposes but not for other purposes, the defense of ultra vires is not available "unless it be shown that the party dealing with the corporation had notice of the intention to perform the act for an unauthorized purpose or under circumstances not justifying its performance."⁹⁸

§ 1594. Application of rule to acquisition of property or borrowing of money. It is no defense to an action to foreclose a corporate mortgage that the money was loaned to the corporation for an ultra vires purpose where the lender had no knowledge thereof.⁹⁹

§ 1595. Application of rule to negotiable instruments—In general. Ultra vires is no defense to an action on a corporate note where the corporation has received the benefits.¹ A corporation having general power to issue negotiable paper cannot set up ultra vires as a defense where it has issued such paper for an unauthorized purpose, as against a holder in due course.² If the payee of a note has no knowledge as to what the money lent was borrowed for, the corporation maker cannot set up that the loan was used for an ultra vires purpose.³ An acceptance

⁹⁶ See § 1511, *supra*.

⁹⁷ *Mellvaine v. Foreman*, 292 Ill. 224, 126 N. E. 749.

⁹⁸ *James Eva Estate v. Mecca Co.*, — Cal. App. —, 181 Pac. 415.

The burden of showing that the corporate act, while within the powers of the corporation for some purposes, is beyond its powers under the circumstances of the particular case, rests upon the corporation denying its liability. *James Eva Estate v. Mecca Co.*, — Cal. App. —, 181 Pac. 415.

⁹⁹ *Albany Sav. Bank v. Kingsbury-Leahy Co.*, — N. Y. Misc. —, 178 N. Y. Supp. 195.

¹ *Burke Brick Co. v. First Nat. Bank*, 249 Fed. 607.

² *M. J. Webb & Co. v. Watkins*, 20 Ga. App. 436, 93 S. E. 108; *Galveston-Houston Interurban Co. v. Dow*, — Tex. Civ. App. —, 193 S. W. 353.

³ *Carter-Mullaly Transfer Co. v. Robertson*, — Tex. Civ. App. —, 198 S. W. 791.

by a bank of a bill of exchange, although ultra vires, is enforceable in the hands of a purchaser for value where the bank received the money therefor.⁴

§ 1596. — Accommodation paper. Ultra vires is no defense to an action on an accommodation indorsement where the corporation has received and retains the benefits of such indorsement.⁵

§ 1599. Distinction as basis for exception to rule as to contracts executed on one side only—Illinois rule. In Illinois, a note of a corporation, whether ultra vires or not, is valid in the hands of a bona fide purchaser without notice.⁶

VIII. OBLIGATION TO RESTORE BENEFITS RECEIVED UNDER ULTRA VIRES CONTRACT: REMEDIES OF PARTIES TO ULTRA VIRES CONTRACT OTHER THAN ACTION ON CONTRACT ITSELF

§ 1602. General rules. Getting money under and by means of an ultra vires act does not justify a corporation in refusing to pay it back and appropriating it.⁷ There is a liability on implied contract to restore benefits received.⁸

§ 1603. Restoration as condition to rescission. A corporation can obtain the rescission of its contract on the ground of ultra vires only where it does equity.⁹

§ 1604. Action on implied contract—In general. The fact that an agreement was ultra vires does not prevent a recovery on implied contract.¹⁰ An action for the money or benefit actually received lies even though the contract was ultra vires and the federal rule as to ultra vires as a defense is applicable

⁴ Sherrill v. American Trust Co., 176 N. C. 591, 97 S. E. 471.

Ins. Co., — Tex. Civ. App. —, 209 S. W. 786.

⁵ In re Prospect Leasing Co., 250 Fed. 707, where nothing is said about bona fide holders in due course.

⁸ National Sales Co. v. Manciet, 83 Ore. 34, L. R. A. 1917 D 485, 162 Pac. 1055.

⁶ American Trust & Savings Bank v. A. Bauer Distilling & Importing Co., 205 Ill. App. 255.

⁹ Shearer v. Farmers' Life Ins. Co., 262 Fed. 861.

⁷ Trammell v. San Antonio Life

¹⁰ England v. Commercial Bank, 242 Fed. 813.

where the transaction is not *malum in se*.¹¹ In case of an implied contract to reimburse, where the express contract is *ultra vires*, the burden is on plaintiff to show the benefits received.¹² A corporation is not liable on an implied contract, in case of an *ultra vires* contract which is itself unenforceable, unless the money or property received thereunder has been beneficially applied to authorized objects or purposes; and hence a bank is not liable for fertilizer sold it where the fertilizer was not used in any legitimate way to carry on the lawful business of the bank within its chartered powers.¹³

§ 1608. Accounting in equity. Property received in connection with an *ultra vires* contract must be accounted for.¹⁴ Where a corporation receives the money or property of another under an agreement or duty to account therefor, it may be compelled to perform such duty, although the transactions were *ultra vires*.¹⁵ A corporation which has received securities by virtue of an *ultra vires* guaranty must account for them.¹⁶ A corporation cannot receive money for bonds, keep the bonds, and then refuse to deliver them on the ground that the contract was *ultra vires*.¹⁷

¹¹ *Gilbert v. Citizens' Nat. Bank*, 61 Okla. 112, 160 Pac. 635; *National Sales Co. v. Manciet*, 83 Ore. 34, L. R. A. 1917 D 485, 162 Pac. 1055; *Dillard & Coffin Co. v. Richmond Cotton Oil Co.*, 140 Tenn. 290, 204 S. W. 758.

¹² *International Harvester Co. v. State Bank*, 38 N. D. 632, 166 N. W. 507.

¹³ *Wiley Fertilizer Co. v. Carroll*, 202 Ala. 335, 80 So. 417.

¹⁴ *Dorothy v. Commonwealth Commercial Co.*, 198 Ill. App. 601, *aff'd* 278 Ill. 629, L. R. A. 1917 E 1110, 116 N. E. 143.

¹⁵ *Laurel County v. Howard*, 189 Ky. 221, 224 S. W. 762.

¹⁶ *Tracy Loan & Trust Co. v. Merchants' Bank*, 50 Utah 196, 167 Pac. 353.

¹⁷ *Chambers, Watson & Watson v. Hines*, — Tex. Civ. App. —, 225 S. W. 200.

CHAPTER 38

ILLEGAL OR PROHIBITED CONTRACTS

- § 1611. Distinguished from ultra vires contracts.
- § 1614. Kinds of illegal contracts—Contracts contrary to public policy.
- § 1615. Effect in general of illegal contracts.
- § 1616. Effect of contracts in violation of charter or statutory prohibition
—General rules.
- § 1617. — Prohibition merely declaratory of common-law doctrine of ultra vires.
- § 1619. — Lending money, discounting and taking securities.
- § 1621. — Limitation of indebtedness.
- § 1623. Relief of party from illegal contract—In general.
- § 1627. — Parties not in *pari delicto*.

§ 1611. Distinguished from ultra vires contracts.¹

§ 1614. **Kinds of illegal contracts—Contracts contrary to public policy.** A corporation is not estopped to set up the defense that the agreement has been prohibited by statute, or is immoral, or is otherwise contrary to public policy, merely because it has been executed by the other party in good faith and the corporation has received the benefits of the contract.² A note of a corporation for an ultra vires purpose and issued in violation of the public policy of the state, where not expressly made “void” by statute, is enforceable in the hands of a bona fide holder.³ A contract between a stockholder suing for a receiver, and a majority stockholder, to dismiss the suit and give no information as to the commencement thereof, is against public policy and void, where made to prevent a prospective purchaser of the corporate property from obtaining knowledge of the facts.⁴

¹ See § 1512, *supra*.

398, 211 S. W. 985, and cases cited therein.

² *West Penn Chemical & Manufacturing Co. v. Prentice*, 236 Fed. 891, 895.

⁴ *Eggleston v. Pantages*, 103 Wash. 458, 175 Pac. 34.

³ See *Washer v. Smyer*, 109 Tex.

§ 1615. **Effect in general of illegal contracts.** Partial illegality of a contract may vitiate all of it.⁵

§ 1616. **Effect of contracts in violation of charter or statutory prohibition—General rules.** Where certain contracts are prohibited by the express language of a statute, the corporation is not liable thereon.⁶ If certain corporate contracts are prohibited by statute, the corporation cannot be held liable on the theory that it has received the benefit of the contract but in such a case the contract is void.⁷ A stockholder, although he owns a large part of the stock, is not individually liable for benefits received by a sale of corporate property by a broker, where the contract between the broker and the corporation violated a statute because not in writing.⁸

Good faith performance of the contract by the other party, while it precludes the defense of *ultra vires*, does not preclude the defense that the contract was expressly forbidden by statute.⁹

§ 1617. — **Prohibition merely declaratory of common-law doctrine of *ultra vires*.** Mere general prohibitions against exceeding corporate powers do not make such acts illegal as well as *ultra vires*.¹⁰

§ 1619. — **Lending money, discounting and taking securities.**¹¹ In California, a loan by a bank in excess of the amount limited by statute is nevertheless enforceable by the bank.¹²

§ 1621. — **Limitation of indebtedness.**¹³ Where stockholders have taken no steps to prevent the corporation exceeding its

⁵ *Moss v. Copelof*, 231 Mass. 513, 121 N. E. 508.

⁶ *Richardson v. Bermuda Land & Live Stock Co.*, — Tex. Civ. App. —, 210 S. W. 746.

⁷ *Richardson v. Bermuda Land & Live Stock Co.*, — Tex. Civ. App. —, 210 S. W. 746.

⁸ *Eaton v. Yount*, — Cal. App. —, 191 Pac. 1009.

⁹ *Palmer v. Scheftel*, 183 N. Y. App. Div. 77, 170 N. Y. Supp. 588.

¹⁰ *Hollis Cotton Oil, Light & Ice Co. v. Marrs & Lake*, — Tex. Civ. App. —, 207 S. W. 367. Contra, *Zurn v. Mitchell*, — Tex. Civ. App. —, 196 S. W. 544.

¹¹ Excessive loan by bank as defense to action by bank to recover loan, see note in 3 A. L. R. 59.

¹² *Blochman Commercial & Savings Bank v. F. G. Investment Co.*, 177 Cal. 762, 171 Pac. 943.

¹³ Note on "Construction of debt limit provision in charter of pri-

debt limit, and the limit has been in fact exceeded, the obligation may be enforced both against the corporation and subsequent creditors, where the benefits of the obligation have accrued to the corporation.¹⁴ In Iowa, however, a debt in excess of the debt limit is void.¹⁵

§ 1623. Relief of party from illegal contract—In general. If a corporate contract is illegal because contrary to a statute, neither party can obtain any relief in court where they are in *pari delicto*.¹⁶

§ 1627. — Parties not in *pari delicto*.¹⁷

vate corporation," see Ann. Cas. 1918 B 966.

¹⁴ *Douglass v. State Bank of Orlando*, — Fla. —, 82 So. 593, discussing the question at some length and criticizing *Bell & Coggeshall Co. v. Kentucky Glass-Works Co.*, 106 Ky. 7, 50 S. W. 2, 1092, 51 S. W. 180.

¹⁵ *Junkin v. Plain Dealer Pub. Co.*, 181 Iowa 1203, 165 N. W. 339.

¹⁶ *In re Springfield Realty Co.*, 257 Fed. 785.

¹⁷ See *Trammell v. San Antonio Life Ins. Co.*, — Tex. Civ. App. —, 209 S. W. 786.

CHAPTER 39

CORPORATE MEETINGS AND ELECTIONS

I. NECESSITY FOR AND CALLING OF MEETINGS

- § 1631. Calling of meetings.
- § 1632. Remedies on refusal to call meetings.

II. TIME AND PLACE OF HOLDING MEETINGS

- § 1633. Time of holding meetings.
- § 1634. Place of holding meetings—In general.
- § 1635. — Meetings held without the state.

III. NOTICE OF MEETINGS

- § 1637. In general.
- § 1639. Statement of business to be transacted.
- § 1641. Waiver, estoppel and ratification.

IV. CONDUCT OF MEETINGS AND ELECTIONS

- § 1643. Quorum.
- § 1645. Inspectors of elections.
- § 1647. Number necessary to decide or elect.
- § 1648. Determination of eligibility of voters.
- § 1650. Voting, count of vote and announcement of result.
- § 1653. Adjournment or postponement.
- § 1655. Effect of failure to attend or withdrawal.

V. THE RIGHT TO VOTE AND PERSONS ENTITLED TO DO SO

- § 1658. Persons entitled to vote—Charter or statutory provisions.
- § 1661. — Stock illegally issued.
- § 1662. — Stockholders having a personal interest.
- § 1663. — Effect of transfers and sales of stock.
- § 1664. — Right to vote as between pledgor and pledgee.
- § 1665. — Stock or transfer books as evidence.
- § 1666. — Trustees and cestuis que trust.
- § 1667. — Executors, administrators, surviving partners.
- § 1673. — Right of corporation to vote its own shares.
- § 1674. — Right to vote shares owned jointly.

VI. NUMBER OF VOTES AND CUMULATIVE VOTING

- § 1682. Cumulative voting.

VII. PROXIES OR POWERS OF ATTORNEY TO VOTE SHARES

§ 1683. In general.

§ 1685. Express restrictions.

§ 1686. Who may give a proxy—In general.

§ 1688. Who may act as proxy.

§ 1689. Form and genuineness of proxies.

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IX. REVIEW AND CONTROL OF ELECTIONS BY COURTS

§ 1699. Quo warranto and mandamus.

§ 1700. Jurisdiction in equity generally.

§ 1702. Injunction against voting or to prevent denial of right.

§ 1704. Statutory remedies.

I. NECESSITY FOR AND CALLING OF MEETINGS

§ 1631. Calling of meetings. There can be no lawful stockholders' meeting unless based on a legitimate call except where all the stock is present and consents to the meeting.¹ It is no good excuse for not calling an annual meeting that some of the stock is in litigation and some of it had been bought in by the corporation to enforce a lien on it.²

If not otherwise provided for, the directors are the proper officers to call the meeting.³ A call for a special meeting to elect directors, where not elected at the annual meeting, by the president, is invalid where the statute requires the meeting to be called by the directors or by any two stockholders, notwithstanding a by-law authorized the president to call such a meeting.⁴

Attendance and participation by all the stockholders waives all objections to the regularity of the call for the meeting or its place.⁵ Where a person, as director, participated in the proceedings directing the calling of a stockholders' meeting, and

¹ Grant v. Elder, 64 Colo. 104, 170 Pac. 198.

² Walsh v. State, 199 Ala. 486, 74 So. 45.

³ Walsh v. State, 199 Ala. 486, 74 So. 45.

Who may call meeting of religious corporation to elect trus-

tees, under Massachusetts statutes, see First African M. E. Society v. Worthy, 232 Mass. 331, 122 N. E. 289.

⁴ Grant v. Elder, 64 Colo. 104, 170 Pac. 198.

⁵ Guaranty Loan Co. v. Fontanel, — Cal. —, 190 Pac. 177.

as secretary he gave notice of such meeting, and as a stockholder participated therein without objection until after the meeting had adjourned, he is estopped from questioning the regularity of the meeting in that it was not legally or regularly called.⁶

§ 1632. Remedies on refusal to call meetings. For refusal to call an annual meeting, mandamus lies.⁷ In Delaware, by statute, the court may, on petition, summarily order a meeting of stockholders to elect directors.⁸

II. TIME AND PLACE OF HOLDING MEETINGS

§ 1633. Time of holding meetings. Where the annual meeting is not called or held on the date prescribed in the by-laws, it is the duty of the directors to call such annual meeting within a reasonable time.⁹ Directors cannot by a change in by-laws so change the time of holding the annual election as to have the effect of continuing themselves in office against the will of the majority of the stockholders.¹⁰ In England, statutes impose a penalty on every director where a general meeting of the stockholders is not held at least once in every calendar year.¹¹

§ 1634. Place of holding meetings—In general. A stockholders' meeting of a railroad company held in a state where it was incorporated, where voting by proxy is allowed, need not be repeated in another state where the company was also incorporated although the law of the latter state does not allow voting by proxy.¹²

§ 1635. — Meetings held without the state. Meetings outside the state cannot be attacked by the corporation or stockholders,

⁶ Smith v. Knauss, — Utah —, 176 Pac. 621.

⁷ Walsh v. State, 199 Ala. 486, 74 So. 45.

⁸ In re Election of Directors of Associated Automatic Sprinkler Co., — Del. —, 102 Atl. 787.

⁹ Walsh v. State, 199 Ala. 486, 74 So. 45.

¹⁰ Walsh v. State, 199 Ala. 486, 74 So. 45.

Power of directors to change time for regular meetings of stockholders, see also note in 2 A. L. R. 558, annotating Walsh v. State, 199 Ala. 486, 2 A. L. R. 551, 74 So. 45.

¹¹ Smedley v. Registrar of Companies, [1919] 1 K. B. 97.

¹² Brown v. Boston & M. Ry., 233 Mass. 502, 124 N. E. 322.

where all the stockholders participate therein.¹³ A statute providing that "every general meeting" of the company shall be held within the province applies only to annual general meetings.¹⁴

Whether corporate elections may be held outside the state depends in some jurisdictions on whether the corporation is one organized for pecuniary profit.¹⁵ In Illinois, in case of corporations not for pecuniary profit, election of trustees outside the state is left to the discretion of the corporation.¹⁶

Officers elected outside the state are at least *de facto* officers.¹⁷

III. NOTICE OF MEETINGS

§ 1637. In general. Notice must be given of special meetings.¹⁸ Under the California statutes, the by-laws may dispense with notice of annual meetings of stockholders.¹⁹ Notice of the annual meeting of stockholders to elect directors need not be given where the place, day and hour are fixed by the regulations adopted by the stockholders.²⁰ Statutes providing for notice of stockholders' meetings do not apply to religious corporations.²¹ In Ohio, notice of a stockholders' meeting need be given only to stockholders of record.²²

§ 1639. Statement of business to be transacted. Notice of a special meeting of stockholders must clearly state the purpose of the meeting.²³ The reason for the statement of the purposes of the meeting in the notice is to advise stockholders of the

¹³ *Ellsworth v. National Home & Town Builders*, 33 Cal. App. 1, 164 Pac. 14.

¹⁴ *Re Lands & Homes of Canada*, 44 Dom. L. Rep. (Can.) 325.

¹⁵ *People v. Grant*, 283 Ill. 291, 119 N. E. 344, aff'g 208 Ill. App. 235.

¹⁶ *People ex rel. Hoyne v. Grant*, 283 Ill. 391, 119 N. E. 344, aff'g 208 Ill. App. 235, holding medical association one not for pecuniary profit.

¹⁷ *Ellsworth v. National Home & Town Builders*, 33 Cal. App. 1, 164 Pac. 14.

¹⁸ *Asbury v. Mauney*, 173 N. C. 454, 92 S. E. 267.

¹⁹ *Guaranty Loan Co. v. Fontanel*, — Cal. —, 190 Pac. 177.

²⁰ *State ex rel. Carpenter v. Kreutzer*, 100 Ohio St. 246, 126 N. E. 54.

²¹ *Uzzell v. McClelland*, 65 Colo. 324, 176 Pac. 304.

²² *In re S. & S. Mfg. & Sales Co.*, 246 Fed. 1005.

²³ *Asbury v. Mauney*, 173 N. C. 454, 92 S. E. 267; *Pacific Coast Coal Mines, Ltd. v. Arbuthnot*, 36 Dom. L. Rep. (Can.) 564.

business to be brought before them, and one who attends cannot complain if the action taken is within the power of the corporation and the meeting and relates to a subject-matter stated in the call.²⁴ Where a notice of a stockholders' meeting stated that the meeting was called for two purposes, and one purpose was voted against and the other for, stockholders unsuccessfully voting against the proposition which carried cannot contend that the proposition which was voted down should not have been included in the call.²⁵

§ 1641. Waiver, estoppel and ratification. Failure to give notice of a stockholders' meeting is waived where all the stockholders are present and thereafter they expressly ratified the action taken at such meeting.²⁶ Irregularity in a corporate meeting for failure to notify all the stockholders is immaterial where the acts at such meeting are afterwards ratified at a subsequent meeting at which all the stockholders were present and of which due notice was given.²⁷ Irregularity in the election of directors does not affect the validity of acts of a stockholders' meeting called by them, so far as stockholders who participated in the meeting are concerned.²⁸ Stockholders whose stock is represented at the meeting cannot object to the form of the notice.²⁹ Stockholders who knowingly recognize the validity of directors' meetings for more than two years are precluded from thereafter attacking their validity on the ground that a certain director took no part therein and had no notice thereof.³⁰

IV. CONDUCT OF MEETINGS AND ELECTIONS

§ 1643. Quorum.³¹

²⁴ *Logie v. Mother Lode Copper Mines Co.*, 106 Wash. 208, 179 Pac. 835.

²⁵ *Logie v. Mother Lode Copper Mines Co.*, 106 Wash. 208, 179 Pac. 835.

²⁶ *Randle v. Walker*, — Ala. App. —, 84 So. 551.

²⁷ *Howard v. Tatum*, 81 W. Va. 561, 94 S. E. 965.

²⁸ *Simon Borg & Co. v. New Orleans City R. Co.*, 244 Fed. 617.

²⁹ *Beggs v. Myton Canal & Irrigation Co.*, — Utah —, 179 Pac. 984.

³⁰ *Berman v. Minneapolis Photo Engraving Co.*, 144 Minn. 146, 174 N. W. 735.

³¹ What constitutes a quorum of an incorporated Masonic Grand Lodge, see *State ex rel. Hundley v. Goodwyn*, 83 W. Va. 255, 98 S. E. 577.

§ 1645. Inspectors of elections.³²

§ 1647. Number necessary to decide or elect. A resolution that corporate debts be paid by the stockholders is not binding on an absent stockholder who refuses to ratify it.³³ If a vote of "three-fourths of all the stockholders" is required to authorize a certain act, it means three-fourths of the number of shares and not of the holders.³⁴

§ 1648. Determination of eligibility of voters. Unless required by the charter or statute, inspectors of election need not examine the stock books to see if the persons voting are registered stockholders, but it is a question of fact whether the requisite number of qualified voters were present and affirmatively voted for a certain resolution.³⁵ The inspectors of election cannot determine the qualifications of stockholders as voters but are bound by the stock certificate book.³⁶ The president cannot determine the qualifications of stockholders as voters at the election.³⁷

§ 1650. Voting, count of vote and announcement of result. If the charter gives a right to demand a poll to "members holding" at least a specified number of shares, joint holders of the specified number of shares may demand a poll without the support of any other member.³⁸ Where, because of a tie, caused by cumulative voting of all the shares on the first ballot, only two of five directors are elected, another ballot should be taken to elect at least a quorum, instead of the old board holding over.³⁹ Where two factions of stockholders hold an equal number of shares, and only two of five directors are elected, one faction cannot, by refusing to vote further and remaining

³² See § 1648, *infra*.

³³ *Asbury v. Mauney*, 173 N. C. 454, 92 S. E. 267.

³⁴ *Simon Borg & Co. v. New Orleans City R. Co.*, 244 Fed. 617, construing Louisiana statute, and see § 1736, *infra*.

³⁵ *General Inv. Co. v. Bethlehem Steel Co.*, 248 Fed. 303, 307.

³⁶ *In re Robert Clarke, Inc.*, 186

N. Y. App. Div. 216, 174 N. Y. Supp. 314.

³⁷ *In re Robert Clarke, Inc.*, 186 N. Y. App. Div. 216, 174 N. Y. Supp. 314.

³⁸ *Siemens Bros. & Co., Ltd. v. Burns*, [1918] 2 Ch. Div. 324.

³⁹ *State ex rel. Price v. Du Brul*, 100 Ohio St. 272, 126 N. E. 87.

silent, thereafter question the election of the other directors on a succeeding ballot by the opposite faction.⁴⁰

§ 1653. Adjournment or postponement. Directors cannot postpone the date of the annual meeting of the stockholders where fixed by the by-laws adopted by the stockholders.⁴¹ Where not required by the by-laws, notice need not be given stockholders of the date of the adjourned annual meeting of the stockholders.⁴²

§ 1655. Effect of failure to attend or withdrawal. One deliberately refraining from attending an election of directors should not be permitted to have the election set aside, especially where a new election would result in injustice.⁴³

V. THE RIGHT TO VOTE AND PERSONS ENTITLED TO DO SO

§ 1658. Persons entitled to vote—Charter or statutory provisions. The charter may deny to preferred stockholders the right to vote.⁴⁴

§ 1661. — Stock illegally issued. The holder of shares of stock void because fictitiously paid up in violation of a constitutional provision cannot vote such stock and have it counted so as to constitute a majority of stock, to the detriment of stockholders who have paid par value and to the benefit of holders of void stock.⁴⁵

§ 1662. — Stockholders having a personal interest. Ordinarily a stockholder is not debarred from voting because of an adverse personal interest,⁴⁶ at least in regard to a question of

⁴⁰ State ex rel. Price v. Du Brul, 100 Ohio St. 272, 126 N. E. 87.

⁴¹ State ex rel. Carpenter v. Kreutzer, 100 Ohio St. 246, 126 N. E. 54.

President of election committee of fraternal beneficiary association held to have no power to postpone meeting for election of officers, in Society of Mutual Succor St. Mary of Lattini of Roccamonfina v. Iacobe, 232 Mass. 263, 122 N. E. 292.

⁴² Mooney v. Farmers' Mercantile & Elevator Co. of Madison, 138 Minn. 199, 164 N. W. 804.

⁴³ In re P. F. Keogh, Inc., 192 N. Y. App. Div. 624, 183 N. Y. Supp. 408.

⁴⁴ Millspaugh v. Cassedy, 191 N. Y. App. Div. 221, 181 N. Y. Supp. 276.

⁴⁵ Bentley v. Zelma Oil Co., 76 Okla. 116, 184 Pac. 131.

⁴⁶ Thurmond v. Paragon Col-

business policy.⁴⁷ A stockholder cannot be deprived of the right to vote because he proposes to use his right for purposes which other stockholders may think not to the best interests, or even to the detriment, of the corporation.⁴⁸

§ 1663. — Effect of transfers and sales of stock. Failure to pay a tax imposed by statute on transfers of stock is no ground for refusing to allow such stock to be voted, where such failure in no way affects the ownership of the stock.⁴⁹ A corporation should not be refused the right to vote its stock on the ground that the stock represented shares transferred within 20 days of the election, where the corporation which held 2,013 shares had disposed of 12 shares to 4 persons and then had a new certificate issued to it for 2,001 shares within such 20 days.⁵⁰

§ 1664. — Right to vote as between pledgor and pledgee. A pledgee may vote stock held by him, although the by-laws provide that no person can vote but the one in whose name the stock appears on the books, where he had had a transfer made on the books to him as collateral.⁵¹

§ 1665. — Stock or transfer books as evidence. The stock book is evidence of the right to vote the stock shown to be in the name of the owner.⁵² Falsity of a stockholder's list which would have been disclosed by a properly kept stock ledger should not deprive a stockholder of the right to vote.⁵³

liery Co., 82 W. Va. 49, 95 S. E. 816.

A stockholder may vote although related to interested persons. *Du Pont v. Du Pont*, 256 Fed. 129, *aff'g* 251 Fed. 937.

⁴⁷ *Du Pont v. Du Pont*, 251 Fed. 937, 944, modified in 256 Fed. 129, distinguishing *Cook v. Deeks*, L. R. App. Cas. 554, relating to misappropriations.

⁴⁸ *Walsh v. State*, 199 Ala. 486, 74 So. 45.

⁴⁹ *In re Election of Directors of Associated Automatic Sprinkler Co.*, — Del. —, 102 Atl. 787.

⁵⁰ *In re Election of Directors of Associated Automatic Sprinkler Co.*, — Del. —, 102 Atl. 787, where court said there was in legal effect a division of the shares into several portions and not a transfer of all and a retransfer of part.

⁵¹ *Hardman v. Barrow*, 147 Ga. 617, 95 S. E. 209.

⁵² *Walsh v. State*, 199 Ala. 486, 74 So. 45.

⁵³ *In re Election of Directors of Associated Automatic Sprinkler Co.*, — Del. —, 102 Atl. 787.

§ 1666. — **Trustees and cestuis que trust.** A trust provision that "my said executors shall vote the said shares of stock at any corporation meeting * * * by their joint action and not otherwise" is mandatory, and while either may vote personally or by proxy they must vote it jointly and cannot vote at all if they disagree as to how to vote.⁵⁴ If trustees cannot agree as to how to vote stock, a court has no power to interfere and direct the voting.⁵⁵ Where shares of stock of another company owned by the mortgagor are covered by a trust deed, the trustees may vote such stock as they please without being obliged to follow the directions of the mortgagor corporation.⁵⁶

§ 1667. — **Executors, administrators, surviving partners.** Representatives of the deceased may vote stock standing on the corporate books in the name of the testator.⁵⁷ On the death of a stockholder, his administrators become vested with the legal title to the stock and are entitled to vote it without a formal transfer on the books.⁵⁸ If legal title to stock is vested in two or more executors, they can only vote as joint owners, and if they cannot agree as to the manner of voting they cannot vote at all.⁵⁹

§ 1673. — **Right of corporation to vote its own shares.** Stock purchased by the corporation to enforce its statutory lien is treasury stock and cannot be voted.⁶⁰ In the absence of an express statute conferring the right, a corporation cannot vote its own stock directly or indirectly through trustees holding it for the use and benefit of the corporation.⁶¹

§ 1674. — **Right to vote shares owned jointly.**⁶²

⁵⁴ *Townsend v. Winburn*, 107 N. Y. Misc. 443, 177 N. Y. Supp. 757.

⁵⁵ *Townsend v. Winburn*, 107 N. Y. Misc. 443, 177 N. Y. Supp. 757.

⁵⁶ *Siemens Bros. & Co., Ltd. v. Burns*, [1918] 2 Ch. Div. 324.

⁵⁷ *Billings v. Marshall Furnace Co.*, 210 Mich. 1, 9 A. L. R. 1239, 177 N. W. 222.

⁵⁸ *Townsend v. Winburn*, 107 N.

Y. Misc. 443, 177 N. Y. Supp. 757.

⁵⁹ *Townsend v. Winburn*, 107 N. Y. Misc. 443, 177 N. Y. Supp. 757.

⁶⁰ *Walsh v. State*, 199 Ala. 486, 74 So. 45.

⁶¹ *Tapper v. Boston Chamber of Commerce*, — Mass. —, 126 N. E. 464.

⁶² See §§ 1666, 1667, *supra*.

VI. NUMBER OF VOTES AND CUMULATIVE VOTING

§ 1682. **Cumulative voting.** In Nebraska the supreme court, while refusing to decide whether the constitutional provision as to cumulative voting for officers is self-executing, held that the statute relating thereto is not unconstitutional because expressly made not applicable to stockholders holding stock in competing corporations.⁶³ In New York, the right to cumulative voting is fixed by statute conditioned on a provision to that effect in the certificate of incorporation; and a provision in such a certificate that stockholders may vote "cumulatively or otherwise" as provided for by the statutes is sufficient to authorize such voting.⁶⁴ The fact that during the many years of the existence of a corporation the cumulative method of voting was never used does not show that such method of voting was not authorized by the certificate of incorporation.⁶⁵ The statutory right to cumulative voting of stock is not limited to one ballot.⁶⁶

VII. PROXIES OR POWERS OF ATTORNEY TO VOTE SHARES

§ 1683. **In general.**⁶⁷ Voting by proxy may be authorized by usage,⁶⁸ and cannot be objected to for the first time in court.⁶⁹ If voting by proxy is not objected to at the time, the objection cannot afterwards be urged.⁷⁰ If the charter authorizes an act upon a vote of the stockholders "representing" a three-fourths majority, voting by proxy is proper.⁷¹ Voting of stock under a proxy from the person in whose name it stands on the corporate books is not conclusive as to ownership of the stock.⁷²

⁶³ State ex rel. Kemper v. Dorchester Farmers' Co-op. Grain & Live Stock Co., 102 Neb. 625, 168 N. W. 643.

⁶⁴ In re Jamaica Consumers' Ice Co., 190 N. Y. App. Div. 739, 180 N. Y. Supp. 384.

⁶⁵ In re Jamaica Consumers' Ice Co., 190 N. Y. App. Div. 739, 180 N. Y. Supp. 384.

⁶⁶ State ex rel. Price v. Du Brul, 100 Ohio St. 272, 126 N. E. 87.

⁶⁷ Definition of proxy, see Man-

son v. Curtis, 223 N. Y. 313, 119 N. E. 559.

⁶⁸ Rossing v. State Bank, 181 Iowa 1013, 165 N. W. 254.

⁶⁹ Rossing v. State Bank, 181 Iowa 1013, 165 N. W. 254.

⁷⁰ Rossing v. State Bank, 181 Iowa 1013, 165 N. W. 254.

⁷¹ Rossing v. State Bank, 181 Iowa 1013, 165 N. W. 254.

⁷² Duquesne Bond Corporation v. American Surety Co., 264 Pa. 203, 107 Atl. 759.

§ 1685. Express restrictions.⁷³ Where the charter provides that proxies shall be deposited with the company not less than two days "before the day for holding the meeting at which the person named in such instrument proposes to vote," proxies deposited after the date of an original meeting but more than two days before the adjourned meeting cannot be used for voting at the adjourned meeting.⁷⁴

§ 1686. Who may give a proxy—In general. A seller of stock who is still registered as a stockholder may vote by proxy.⁷⁵ The purchaser of shares of stock may secure the right to vote from his vendor by means of a proxy, although the purchaser is not yet registered as a stockholder.⁷⁶ The voting of proxies given by stockholders of record who have transferred their shares does not invalidate the acts done at a stockholders' meeting.⁷⁷

§ 1688. Who may act as proxy. An officer of a corporation may act as proxy.⁷⁸ Statutes in some states prohibit officers of an insurance company from voting proxies at the annual stockholders' meeting unless authorized to do so by a majority of the trustees; but thereunder the trustees cannot restrict the right to vote by proxy to certain questions, and if they do so the officers may vote the proxies on all questions.⁷⁹

§ 1689. Form and genuineness of proxies. Proxies not stamped as required by the Federal Revenue Act of 1919 are properly rejected as votes cast for the election of directors, the statute making them "invalid and of no effect."⁸⁰

§ 1691. Power of court to compel execution of a proxy. A trustee, in case of a dry trust, must give a proxy.⁸¹

⁷³ Forbidding solicitation of proxies in case of insurance companies, see *State v. Meredith*, 183 Iowa 783, 167 N. W. 626.

⁷⁴ *McLaren v. Thomson*, [1917] 2 Ch. Div. 261.

⁷⁵ *Thompson v. Blaisdell*, — N. J. L. —, 107 Atl. 405.

⁷⁶ *Thompson v. Blaisdell*, — N. J. L. —, 107 Atl. 405.

⁷⁷ *In re S. & S. Manufacturing & Sales Co.*, 246 Fed. 1005.

⁷⁸ *State v. Meredith*, 183 Iowa 783, 167 N. W. 626.

⁷⁹ *State ex rel. Lally v. Cadigan*, 103 Wash. 254, 174 Pac. 965.

⁸⁰ *State ex rel. Hemey v. Miller*, — Wis. —, 179 N. W. 815.

⁸¹ *Thompson v. Blaisdell*, — N. J. L. —, 107 Atl. 405.

§ 1692. Authority of proxies and effect of representation.

A general proxy does not authorize the holder to vote to sell all the corporate assets.⁸² Giving a proxy to vote at a stockholders' meeting against appealing from a winding up order made in Canada does not confer jurisdiction on the Canadian court, as against such stockholder, so as to permit it to render a personal judgment against him.⁸³ The stockholder may give secret instructions to his proxy as to the mode of voting on certain questions.⁸⁴ Where a statute provides that no officer of the company "shall be allowed to vote the proxy of any stockholder or member" unless "the majority of the trustees vote to permit such action," the trustees, while they have a right to refuse to allow the officers to vote proxies, cannot limit the use of the proxies so as to perpetuate themselves in office and limit interference with the business.⁸⁵

Objections to acts of a proxy must be made promptly.⁸⁶ If a stockholder who gives a proxy does not promptly object, he cannot urge that the proxy did not authorize the holder to vote as to dissolution of the corporation.⁸⁷

A report at a stockholders' meeting, showing ownership of bank stock, does not impute notice to stockholders represented by proxy that the stock was acquired *ultra vires*.⁸⁸

§ 1694. Revocation or termination of power. Even if a sale of stock is a technical revocation of a proxy given the buyer by the seller, the seller need not execute a new proxy where both the buyer and seller are content with the control of the voting power given by the title shown on the transfer books accompanied by the proxy.⁸⁹ A contract between majority stockholders to vote for each other for directors is not void as an attempt to confer on the daughter of one of the stockholders an irrevocable proxy, nor is it a testamentary disposition because

⁸² *Shield v. Lone Star Life Ins. Co.*, — Tex. Civ. App. —, 202 S. W. 211.

⁸³ *Traders' Trust Co. v. Davidson*, — Minn. —, 178 N. W. 735.

⁸⁴ *State ex rel. Lally v. Cadi-gan*, 103 Wash. 254, 174 Pac. 965.

⁸⁵ *State ex rel. Lally v. Cadi-gan*, 103 Wash. 254, 174 Pac. 965, construing Insurance Code.

⁸⁶ *Rossing v. State Bank*, 181 Iowa 1013, 165 N. W. 254.

⁸⁷ *Rossing v. State Bank*, 181 Iowa 1013, 165 N. W. 254.

⁸⁸ *Holmes v. Crane*, 191 N. Y. App. Div. 820, 182 N. Y. Supp. 270.

⁸⁹ *Thompson v. Blaisdell*, — N. J. L. —, 107 Atl. 405.

it provides that on the death of one of the stockholders his daughter should have the power to vote the stock and should pay to his other two children their share of the stock, where the contract was irrevocable.⁹⁰ Contracts of majority stockholders by which they agree to vote for certain persons for directors so as to secure to themselves the control of the corporation are not illegal so long as no fraud is committed on the corporation nor wrong done to the other stockholders.⁹¹

IX. REVIEW AND CONTROL OF ELECTIONS BY COURTS

§ 1699. **Quo warranto and mandamus.**⁹² A statute authorizing quo warranto against any person who usurps, intrudes into, or unlawfully holds or exercises "any franchise" permits quo warranto to be brought where the validity of a corporate election is in dispute and the only question is as to the title of holdover directors against newly-elected directors.⁹³ Mandamus is a proper remedy to determine the validity of a corporate election of officers.⁹⁴

§ 1700. **Jurisdiction in equity generally.** Title to corporate office cannot ordinarily be determined by a bill in equity.⁹⁵ A suit in equity to restrain persons from acting as directors of a private corporation, where they have been irregularly elected, is not proper in the absence of special legislation.⁹⁶ Laches may bar a suit to try the validity of a corporate election.⁹⁷

Equity has jurisdiction where the validity of the election of officers is merely incidental to the relief sought upon other grounds.⁹⁸ A bill in equity should not be dismissed on the

⁹⁰ *Thompson v. J. D. Thompson Carnation Co.*, 279 Ill. 54, Ann. Cas. 1917 E 591, 116 N. E. 648.

⁹¹ *Thompson v. J. D. Thompson Carnation Co.*, 279 Ill. 54, Ann. Cas. 1917 E 591, 116 N. E. 648.

⁹² Quo warranto as remedy to try title to office, and procedure therein, see *Com. v. Luker*, 258 Pa. 602, 102 Atl. 276.

⁹³ *Grant v. Elder*, 64 Colo. 104, 170 Pac. 198.

⁹⁴ *Society of Mutual Succor St.*

Mary of Lattini of Roccamonfina v. Iacobe, 232 Mass. 263, 122 N. E. 292.

⁹⁵ *Grant v. Elder*, 64 Colo. 104, 170 Pac. 198.

⁹⁶ *Grant v. Elder*, 64 Colo. 104, 170 Pac. 198.

⁹⁷ *Grant v. Elder*, 64 Colo. 104, 170 Pac. 198.

⁹⁸ *Society of Mutual Succor St. Mary of Lattini of Roccamonfina v. Iacobe*, 232 Mass. 263, 122 N. E. 292; *Hammer v. Cash*, — Wis.

theory that the validity of a corporate election is involved where such validity is merely incidental to the relief sought upon other grounds.⁹⁹ Equity has jurisdiction to determine the election or qualification of directors or the propriety of the conduct of their meetings outside the state, where such questions arise collaterally in a suit to restrain the illegal forfeiture of complainant's stock.¹

Motives of stockholders in voting a particular way cannot be inquired into by the courts.²

§ 1702. Injunction against voting or to prevent denial of right. Majority stockholders may be enjoined from voting their stock only in case of imperative necessity.³ A stockholder is an indispensable party to a suit seeking to enjoin him from voting his stock at a stockholders' meeting.⁴

§ 1704. Statutory remedies. In New York, the court, in such summary proceeding, cannot declare certain persons elected as directors but should order a new election.⁵ In such a summary proceeding, the court has no power to try summarily by affidavit or like proof the legal and equitable rights involved in the promotion and conduct of corporations between a promoter, the corporation, or its officers, or its stockholders.⁶ The corporation is a necessary defendant to a proceeding to set aside an election of directors.⁷

In Delaware, under the statute authorizing a court of chancery to summarily order a corporate election, the relief granted may, instead of ordering a new election, order that a new return of the election be made showing the counting of the only ballot, which was erroneously rejected, and the election of the

—, 178 N. W. 465, citing Fletcher Cyc. Corp. § 1829.

⁹⁹ *Society of Mutual Succor St. Mary of Lattini of Roccamonfina v. Iacobe*, 232 Mass. 263, 122 N. E. 292.

¹ *Lippman v. Kehoe Stenograph Co.*, — Del. —, 102 Atl. 988.

² *Du Pont v. Du Pont*, 251 Fed. 937, 945, modified 256 Fed. 129.

³ *Davidson v. American Blower Co.*, 243 Fed. 167.

⁴ *General Inv. Co. v. Lake Shore & M. S. Ry. Co.*, 250 Fed. 160, aff'g 226 Fed. 976.

⁵ *In re Robert Clarke, Inc.*, 186 N. Y. App. Div. 216, 174 N. Y. Supp. 314.

⁶ *In re Robert Clarke, Inc.*, 186 N. Y. App. Div. 216, 174 N. Y. Supp. 314.

⁷ *In re P. F. Keogh, Inc.*, 192 N. Y. App. Div. 624, 183 N. Y. Supp. 408.

directors named thereon.⁸ In Delaware where, by statute, the chancellor may summarily order that an election of directors be held, such relief will not be granted where it appears that the annual election has in fact been held on the day designated by the by-laws, although after such election shares voted had been judicially canceled.⁹

The New Jersey statute providing a summary proceeding to review corporate elections applies only to election of directors and does not apply to the appointment or election of a manager or any agent.¹⁰

⁸ *In re Election of Directors of Associated Automatic Sprinkler Co.*, — Del. —, 102 Atl. 787.

⁹ *Schultz v. Commonwealth Mortg. Co.*, — Del. —, 107 Atl. 774.

¹⁰ *Robak v. Polish Businessmen's Inv. Ass'n*, — N. J. L. —, 111 Atl. 599.

CHAPTER 40

VOTING TRUSTS

§ 1705. Definition and general considerations.

§ 1706. Form, manner of creating and execution of agreement.

§ 1707. Validity—In general.

§ 1709. — Public policy as affecting validity—In general.

§ 1710. — — Statutory provisions.

§ 1712. — As dependent upon purpose—Control of policy and management.

§ 1717. Revocability.

§ 1718. Trustees.

§ 1719. Effect upon rights of stockholders.

§ 1721. Remedies.

§ 1705. Definition and general considerations.¹ There is no voting trust where each party to the agreement retains the voting power of his stock.² If a voting trust fails, for any reason, then, of course, the stock reverts to the owners.³

§ 1706. Form, manner of creating and execution of agreement. Of course the duration of the voting trust cannot be extended without the consent of the parties.⁴

§ 1707. Validity—In general.⁵ Voting trust agreements "are valid and binding if based upon a sufficient consideration, if they do not contravene public policy or a positive prohibitory statute, and if they do not sound in fraud or wrong against the stockholders."⁶ A voting trust voluntarily created as a

¹ Voting trusts, see generally *Vintroux v. Chilton*, — W. Va. —, 100 S. E. 496.

² *Manson v. Curtis*, 223 N. Y. 313, Ann. Cas. 1918 E 247, 119 N. E. 559, aff'g 171 N. Y. App. Div. 954, 155 N. Y. Supp. 1123.

³ *Duquesne Bond Corporation v. American Surety Co.*, 264 Pa. 203, 107 Atl. 759.

⁴ *Waters v. De Mossin*, 176 N. Y. App. Div. 711, 164 N. Y. Supp. 82.

⁵ Legality of voting trusts, see article in 18 *Columbia L. Rev.* 123-136.

Validity and effect of provisions in will to control voting power of corporate stock, see note in 9 *A. L. R.* 1242, annotating *Billings v. Marshall Furnace Co.*, 210 Mich. 1, 9 *A. L. R.* 1239, 177 N. W. 222.

⁶ *Clark v. Foster*, 98 Wash. 241, 167 Pac. 908.

condition precedent to a loan to protect the lenders is based on a sufficient consideration.⁷ A voting trust of a submarine boat company, to protect the stock from purchase by agents of the German government during the war, is valid.⁸ Voting trusts for ten years, on turning over the corporate assets or the proceeds to a new company to be formed, where the trust is an active one, are valid.⁹ A voting trust agreement valid in New York where the company was created, is valid, it seems, in Illinois, where its principal place of business was located.¹⁰

§ 1709. — Public policy as affecting validity—In general. In Washington, in considering the validity of voting trusts, after reviewing the conflict in the decisions, it is said that in most of the cases, the courts “have, notwithstanding certain broad statements, inclined to look to the facts and equities of the particular case”; and it was held that a voting trust created by majority stockholders in good faith and to obtain a loan for the corporation, for the apparent advantage of all the stockholders and to protect the loan, to continue for twenty years unless the preferred stock was all redeemed and the bonded debt paid prior to that time, was not against public policy.¹¹

§ 1710. — Statutory provisions. A voting trust agreement does not contravene a statute providing for the voting of stock by the shareholder, etc. In other words, since the statute gives a right to vote by proxy, a shareholder may grant that which is in effect an irrevocable proxy for a definite term of years.¹²

§ 1712. — As dependent upon purpose—Control of policy and management. A provision of a will attempting to create a voting trust for a fixed period, and to exclude for a fixed time the testator’s representatives from management of corporate

⁷ Clark v. Foster, 98 Wash. 241, 167 Pac. 908.

⁸ Frost v. Carse, — N. J. L. —, 108 Atl. 642.

⁹ Irons v. Croft Hat & Notion Co., — W. Va. —, 104 S. E. 111.

¹⁰ In re O’Gara Coal Co., 260 Fed. 742, mining coal in Illinois.

¹¹ Clark v. Foster, 98 Wash. 241, 167 Pac. 908, following Winsor v. Commonwealth Coal Co., 63 Wash. 62, 33 L. R. A. (N. S.) 63, 114 Pac. 908.

¹² Clark v. Foster, 98 Wash. 241, 167 Pac. 908.

affairs, and to perpetuate certain persons in office and control of the company without regard to the rights of minority stockholders, is void as contrary to public policy.¹³

§ 1717. Revocability. Assignments of stock in blank executed and delivered by the voting trustees are sufficient to transfer the title back although they were not, when executed, attached to the several stock certificates.¹⁴

§ 1718. Trustees. Trustees of what in effect was a voting trust for ten years, the corporate assets being turned over to a new corporation to be formed in exchange for part of its stock, have power to pledge such stock so issued to secure payment for the stock.¹⁵ Where a stockholder deposited his stock with the trustee of a voting trust, and the trustee violated his duty by delivering such stock to another who obtained a new certificate issued to himself, the trustee was guilty of conversion and liable for its return or its value.¹⁶ The doctrine of clean hands is applicable to a suit by one trustee of a voting trust to remove another trustee because of corruption of public officials.¹⁷ A trustee of a voting trust should not be removed on the ground of his extravagance or corruption in the absence of reasonably positive and convincing proof.¹⁸ In a suit by a trustee of a voting trust to remove another trustee, a corporation which is the beneficiary of the trust should be made a party as well as the other trustees.¹⁹ In case of a vacancy of a trustee in a voting trust, it should be filled by the beneficiaries and not by the court.²⁰

§ 1719. Effect upon rights of stockholders. If the trust agreement fails, the stock reverts to the owners.²¹

¹³ *Billings v. Marshall Furnace Co.*, 210 Mich. 1, 9 A. L. R. 1239, 177 N. W. 222.

¹⁴ *Duquesne Bond Corporation v. American Surety Co.*, 264 Pa. 203, 107 Atl. 759.

¹⁵ *Irons v. Croft Hat & Notion Co.*, — W. Va. —, 104 S. E. 111.

¹⁶ *Schaad v. Barceloux*, — Cal. App. —, 183 Pac. 716.

¹⁷ *Frost v. Carse*, — N. J. L. —, 108 Atl. 642.

¹⁸ *Frost v. Carse*, — N. J. L. —, 108 Atl. 642.

¹⁹ *Frost v. Carse*, — N. J. Eq. —, 108 Atl. 641.

²⁰ *Frost v. Carse*, — N. J. L. —, 108 Atl. 642.

²¹ *Duquesne Bond Corporation v. American Surety Co.*, 264 Pa. 203, 107 Atl. 759.

§ 1721. Remedies. An action to cancel a voting trust is one in rem so as to authorize constructive service on a nonresident trustee.²² In a suit by a stockholder to cancel a voting trust, an agent who is to be employed under the agreement as a sales agent is a necessary party.²³

²² *Le Roy Sargent & Co. v. McHarg*, — S. D. —, 174 N. W. 742.

²³ *Consolidated Textile Co. v. Dickey*, 266 Fed. 587.

CHAPTER 41

MANAGEMENT AND CONTROL IN GENERAL

§ 1726. Powers of stockholders—In general.

§ 1727. — As an individual acting alone.

§ 1728. — Where owner or owners of all or majority of stock act.

§ 1730. Powers of directors—Powers as individuals.

§ 1732. Powers of officers or agents other than directors—Powers as affected by ownership of large part or all of stock.

§ 1733. Control of directors by stockholders—General rules.

§ 1736. Requirement of consent of stockholders—Necessity created by statute or charter.

§ 1726. Powers of stockholders—In general. When a corporation consists of a small number of persons, they may effectually transact their business in a very informal manner.¹ The president and secretary have no power to act, merely because so directed at a stockholders' meeting, to issue certificates of stock in consideration of a transfer of water rights, where the directors refused to permit such officers to issue such stock, since the corporate management is in the hands of the directors rather than the stockholders.² Stockholders cannot sell corporate property unless either the formal act of a meeting or unless concurred in by all the individual stockholders.³ The stockholders, as distinguished from the directors, may sell all the corporate property, where it is not shown that the control and management of the corporation are not vested in the stockholders.⁴

§ 1727. — As an individual acting alone. A contract made by a stockholder in his own name does not bind the corpora-

¹ Chard v. Ryan-Parker Const. Co., 182 N. Y. App. Div. 455, 169 N. Y. Supp. 622.

³ Jones v. Nichols, 202 Ala. 233, 80 So. 71.

² Anderson v. Grantsville North Willow Irrigation Co., 51 Utah 137, 169 Pac. 168.

⁴ Carrier v. Dixon, 142 Tenn. 122, 218 S. W. 395.

tion.⁵ An agreement between a stockholder and a financial backer is not binding on the corporation nor on purchasers of stock, without notice, from other stockholders.⁶ A stockholder cannot transfer the good will of a corporation.⁷

§ 1728. — Where owner or owners of all or majority of stock act. A stockholder owning half the stock cannot transfer the corporate assets.⁸ A corporation is not a "one-man" one where a syndicate owns a quarter of the stock and holds the rest as security, so as to be bound by contracts made by the owner of three-fourths of the stock.⁹ No one but creditors can complain of the acts of a stockholder in a "one-man" corporation, and hence only creditors at the time he drew corporate checks payable to his personal creditors can complain.¹⁰ Strangers cannot question a conveyance by a sole stockholder as constituting a conveyance of corporate property.¹¹

§ 1730. Powers of directors—Powers as individuals. One of two directors has no power to transfer all the corporate property as security for a debt.¹²

§ 1732. Powers of officers or agents other than directors—Powers as affected by ownership of large part or all of stock. Where there are no creditors and all the stock is owned by an officer, third persons cannot question the title to the corporate property transferred by such officer, without regard to whether a sole stockholder may transfer the corporate property.¹³ In one case it is held that although the president of a corporation had no power to deed the corporate property, yet inasmuch as he owned three-fifths of the stock a three-fifths

⁵ *Feenaughty v. Beall*, 91 Ore. 654, 178 Pac. 600, and see § 26 et seq., *supra*.

⁶ *Elkhorn By-Product Coal Co. v. Tynes*, 188 Ky. 269, 221 S. W. 514.

⁷ *Wylie v. Wylie Permanent Camping Co.*, — Mont. —, 187 Pac. 279.

⁸ *Snyder v. Bender*, 173 N. Y. Supp. 401, and see §§ 23-28, *supra*.

⁹ *Chard v. Ryan-Parker Const.*

Co., 182 N. Y. App. Div. 455, 169 N. Y. Supp. 622.

¹⁰ *Scales v. Holje*, — Cal. App. —, 183 Pac. 308.

¹¹ *Safford v. Tibbetts*, 104 Kan. 224, 178 Pac. 618.

¹² *Snyder v. Bender*, 173 N. Y. Supp. 401, and see § 1854 et seq., *infra*.

¹³ *Safford v. Tibbetts*, 104 Kan. 224, 178 Pac. 618.

interest in the property was thereby conveyed.¹⁴ If an officer owns all the stock, it cannot be contended by persons who had ceased to be stockholders that he could not acquire title to the corporate real property by adverse possession.¹⁵

§ 1733. Control of directors by stockholders—General rules. Courts will not interfere to control the discretion lodged in the directors in regard to the internal management of the corporation, except in case of fraud or where the directors are acting in excess of their powers.¹⁶

§ 1736. Requirement of consent of stockholders—Necessity created by statute or charter. A lease is an "incumbrance" within the statute requiring consent of stockholders to incumbrances.¹⁷ Employing a broker to sell church lands is not a "contract in relation to land" within the charter of a church requiring a majority of the male members of the church to consent to such contracts.¹⁸ Where ratification by stockholders of a corporate contract is necessary, the stockholders are the only parties who can urge the want of ratification.¹⁹ A stranger cannot urge invalidity of a corporate mortgage because not consented to by stockholders.²⁰ Neither a director who made a contract, nor his surety, can attack the contract on the ground that it was not authorized by two-thirds of the stock.²¹ Dissenting minority stockholders of an irrigating company, objecting to corporate transfers, must follow the statutory procedure in relation to an irrigation company.²²

¹⁴ *Bunn v. City of Laredo*, — Tex. Civ. App. —, 213 S. W. 320.

¹⁵ *Safford v. Tibbetts*, 104 Kan. 224, 178 Pac. 618.

¹⁶ See § 4065, *infra*.

¹⁷ *Elder v. Western Min. Co.*, 237 Fed. 966.

¹⁸ *Stablein v. Hutterische Gemeinde*, — S. D. —, 177 N. W. 810.

¹⁹ *United States Industrial Alcohol Co. v. Distilling Co.*, 89 N.

J. Eq. 177, 104 Atl. 216, *aff'g* (N. J. Ch.), 100 Atl. 620.

²⁰ *Day v. Jade Contracting Co.*, — N. Y. Misc. —, 181 N. Y. Supp. 740.

²¹ *Amos v. Continental Trust Co.*, 22 Ga. App. 348, 95 S. E. 1025.

²² *Canyon Creek Irrigation Dist. v. Martin*, — Mont. —, 159 Pac. 418.

CHAPTER 42

DIRECTORS, OTHER OFFICERS AND AGENTS

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§ 1740. Distinction between "officers" and mere "agents"—
In general. An officer of a corporation may or may not be an "employee" within the Workmen's Compensation Act. The size of the corporation and the nature of his duties are the test.¹ A director may be also an employee within the Workmen's Compensation Act.² A person cannot be denied compensation under the Workmen's Compensation Act as an "employee" merely because he happens to be the president or other executive or managing officer of the corporation employing him.³

§ 1743. Who are officers—In general. A master of a vessel is not a "managing officer."⁴ Heads of departments are employees notwithstanding they own stock and are advertised as "officers" in a book of general reference issued by the company.⁵

§ 1745. — Directors as officers.⁶ Incorporation papers and by-laws often clearly show by their terms that the word "officers" as used therein was not intended to include directors.⁷

§ 1749. Number of directors.⁸ The number of directors can be increased only by following the statute in regard thereto.⁹

§ 1753. Validity of agreements relating to corporate offices—In general. It is "not illegal or against public policy for two or more stockholders owning the majority of the shares of stock to make an agreement for the purpose of obtaining control

¹ *In re Raynes*, — Ind. App. —, 118 N. E. 387.

² *Millers' Mut. Casualty Co. v. Hoover*, — Tex. Civ. App. —, 216 S. W. 475.

³ *In re Raynes*, — Ind. App. —, 118 N. E. 387.

Officers as "employees" within workmen's compensation statutes, see further note in L. R. A. 1918 F 201, 203.

⁴ *The Erie Lighter* 108, 250 Fed. 490.

⁵ *Clark v. New England Tele-*

graph & Telephone Co., 231 Mass. 546, 121 N. E. 497.

⁶ Director as "officer" within bankruptcy act, see *Boyd v. Applewhite*, — Miss. —, 84 So. 16.

⁷ *State ex rel. Hemey v. Miller*, — Wis. —, 179 N. W. 815.

⁸ Mode of reducing number of directors in Ohio, see *In re S. C. S. Manufacturing & Sales Co.*, 246 Fed. 1005.

⁹ *Cabana v. Holstein-Friesian Ass'n*, — N. Y. Misc. —, 182 N. Y. Supp. 658.

of the corporation by the election of particular persons as directors.”¹⁰ A contract between stockholders representing a majority of the stock, as to corporate policy or action or as to the officers whom they will elect, where based on a consideration, is valid if not contravening any charter or statutory provision and not contemplating any fraud or wrong against other stockholders or other illegal object.¹¹ But directors cannot contract to elect a designated person as an officer of the bank for a specified time at a specified salary, since in violation of the fiduciary relation.¹² A contract between three of the four stockholders in two newspaper companies that during their lives one of them as president and another as vice president or director were to have the management of the companies, and that the third stockholder joining in the agreement should always vote to retain the other two in office, is against public policy as bargaining away the right to vote for directors.¹³

§ 1754. — Agreements abdicating or limiting powers or discretion of directors or other officers. An agreement between stockholders to secure a merely passive directorate is against public policy and void.¹⁴ As said by Justice Collin of the New York Court of Appeals, “the law does not permit the stockholders to create a sterilized board of directors.”¹⁵ For instance, a contract to organize a corporation merely as a selling agency, to be bound by prices dictated by the seller, has been held void as against public policy as an attempt to deprive the board of directors of the corporation to be organized of the free exercise of their judgment as to the corporate business.¹⁶ So an agreement between holders of a majority of the stock to elect a dummy board of directors and president and that the

¹⁰ *Manson v. Curtis*, 223 N. Y. 313, Ann. Cas. 1918 E 247, 119 N. E. 559, aff'g 171 N. Y. App. Div. 954, 155 N. Y. Supp. 1123.

¹¹ *Manson v. Curtis*, 223 N. Y. 313, Ann. Cas. 1918 E 247, 119 N. E. 559, aff'g 171 N. Y. App. Div. 954, 155 N. Y. Supp. 1123.

¹² *Van Slyke v. Andrews*, — Minn. —, 178 N. W. 959.

¹³ *Haldeman v. Haldeman*, 176 Ky. 635, 197 S. W. 376.

¹⁴ *Manson v. Curtis*, 223 N. Y. 313, Ann. Cas. 1918 E 247, 119 N. E. 559.

¹⁵ *Manson v. Curtis*, 223 N. Y. 313, Ann. Cas. 1918 E 247, 119 N. E. 559.

¹⁶ *Rosenthal v. Light*, 185 N. Y. App. Div. 430, 173 N. Y. Supp. 743.

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management should be vested in one of the stockholders solely and exclusively for a certain period is illegal and void regardless of the good faith of the parties.¹⁷

II. ELECTION OR APPOINTMENT

§ 1759. By whom to be elected or appointed—In case of vacancy in board of directors. Irregularity in a change of the number of directors or the election to fill vacancies is immaterial, so far as the validity of a resolution by the directors is concerned, where all the stockholders ratified such resolution.¹⁸

§ 1761. Time and mode—In case of elections by stockholders. A charter provision as to the date of electing officers is not mandatory in the sense that the corporation cannot postpone the election to a later date.¹⁹ Election of corporate officers cannot be attacked for fraud unless it is shown that a sufficient number of votes was affected thereby to determine the election.²⁰ Breach of trust is not ground for setting aside an election of directors where it is not shown that the alleged breach of trust swung a sufficient number of votes to determine the election.²¹

§ 1763. Mandamus to compel election. Mandamus lies to compel calling of a meeting to elect directors.²²

§ 1764. Effect of election of less than required number of directors. Where a corporation has five directors, an election of four directors instead of five, where otherwise valid, entitles those elected to hold office.²³

§ 1765. Who may question. A stockholder who participates in a stockholders' meeting without objection is estopped to ques-

¹⁷ *Manson v. Curtis*, 223 N. Y. 313, Ann. Cas. 1918 E 247, 119 N. E. 559, aff'g 171 N. Y. App. Div. 954, 155 N. Y. Supp. 1123.

¹⁸ *In re S. & S. Manufacturing Sales Co.*, 246 Fed. 1005.

¹⁹ *Barker v. National Life Ass'n*, 183 Iowa 966, 166 N. W. 597.

²⁰ *In re O'Gara Coal Co.*, 260 Fed. 742.

²¹ *In re O'Gara Coal Co.*, 260 Fed. 742.

²² *Walsh v. State*, 199 Ala. 486, 74 So. 45.

²³ *State ex rel. Price v. Du Brul*, 100 Ohio St. 272, 126 N. E. 87.

tion the legality of the election of directors at such meeting or the act of the directors in electing his successor as secretary of the corporation.²⁴ The legality of an election of directors cannot be attacked after a long delay.²⁵

§ 1767. Appointment of agents. Statutes requiring an "agent's" authority to execute a contract in writing to be itself in writing, do not apply to executive officers of corporations.²⁶ The rule that the declarations of an agent are, as against his principal, inadmissible to prove the fact of his agency does not apply to his testimony as a witness on the trial in which such fact is in issue.²⁷

§ 1768. Presumptions in favor of title to office. There is no presumption that officers acted as such prior to a resolution stating that named individuals are corporate officers and authorized to act for the corporation.²⁸

III. QUALIFICATIONS AND ELIGIBILITY

§ 1769. General rules. Eligibility of a bank cashier as dependent on ownership of stock is presumed in the absence of a showing to the contrary.²⁹

§ 1770. Power to make by-laws as to eligibility. The legislature may confer authority on the corporation to prescribe by by-laws additional or other qualifications than those prescribed by law in case of directors.³⁰

§ 1771. Necessity that director be a stockholder—In general.³¹ A director need not be a stockholder unless the charter or a by-law so requires.³²

²⁴ *Smith v. Knauss*, — Utah —, 176 Pac. 621, and see § 1641, *supra*.

²⁵ *In re O'Gara Coal Co.*, 260 Fed. 742.

²⁶ *Arnold v. La Belle Oil Co.*, — Cal. App. —, 190 Pac. 815.

²⁷ *Raftis v. McCloud River Lumber Co.*, 35 Cal. App. 397, 170 Pac. 176.

²⁸ *Johnson Bros. Lighterage Co. v. American Union Line*, 110 N. Y. Misc. 326, 180 N. Y. Supp. 460.

²⁹ *Hess v. Kismet State Bank*, 106 Kan. 701, 189 Pac. 919.

³⁰ *Johnson v. York Coal & Coke Co.*, 182 Ky. 303, 206 S. W. 611.

³¹ Right of directors in Boston Chamber of Commerce to vote, where not holding certificates of membership, see *Tapper v. Boston Chamber of Commerce*, — Mass. —, 126 N. E. 464.

³² *Parsons v. Rinard Grain Co.*, — Iowa —, 173 N. W. 276; *John-*

§ 1772. — Nominal stockholder or holder of legal title without beneficial ownership. Even if one holding stock under a naked trust is qualified for a director, he is not so qualified "if the stock was put in his name colorably only, and with a view to qualify him as director in furtherance of some dishonest or fraudulent scheme touching the management or control of the company."³³

§ 1776. — Subsequent acquisition of stock. It is sufficient that a director qualifies himself by becoming a holder of the requisite number of shares before he enters upon the office although he holds none at the time of his election.³⁴

§ 1777. — Effect of disposing of stock after election.³⁵ A director is not disqualified by assigning his qualification stock in blank where the transfer was not made on the books and where there was no intention to transfer the stock and disqualify him as a director.³⁶

§ 1778. Residence or citizenship. Residence is often made, by by-laws or the incorporation papers, a necessary qualification for an officer.³⁷

§ 1783. Effect of want of eligibility. The objection that none of the directors were residents of the state where the corporation was created—the statute requiring at least one to be such a resident—can be urged only by the state and not in any proceeding between a corporation and its stockholders.³⁸ A secretary who wrongfully refused to transfer stock to persons elected directors cannot claim they are ineligible because not stockholders.³⁹

son v. York Coal & Coke Co., 182 Ky. 303, 206 S. W. 611.

³³ Johnson v. York Coal & Coke Co., 182 Ky. 303, 206 S. W. 611.

³⁴ Lippman v. Kehoe Stenograph Co., — Del. —, 102 Atl. 988.

³⁵ See also § 1806, *infra*.

³⁶ Lippman v. Kehoe Steno-

graph Co., — Del. —, 102 Atl. 988.

³⁷ State ex rel. Hemey v. Miller, — Wis. —, 179 N. W. 815.

³⁸ Lippman v. Kehoe Stenograph Co., — Del. —, 102 Atl. 988.

³⁹ Guaranty Loan Co. v. Fontanel, — Cal. —, 190 Pac. 177.

IV. ACCEPTANCE OF OFFICE, BOND AND OATH OF OFFICE

§ 1787. Bonds—General considerations.⁴⁰ A fidelity bond is a “contract or policy of insurance” as that term is used in the statutes.⁴¹

§ 1794. — What constitutes breach of bond.⁴² If annual renewals of a bond insuring the fidelity of a bank cashier are made in consideration of a false statement that the cashier was not then in default, the surety company is not liable on such renewals.⁴³

§ 1797. — Notice to sureties of misconduct after execution of bond. Notice to the surety company, as required by the bond of a bank cashier, is not necessary in case of mere suspicion of misconduct of the cashier nor where the only officers having knowledge of embezzlement by the cashier participated in or connived at his offense.⁴⁴

§ 1798. — Duration of liability on bond. A bond of indemnity covering the acts of a cashier “at all times hereafter” is a continuing obligation covering the entire term of employment, where the term was an indefinite one.⁴⁵ If the term of

⁴⁰ See generally *Maryland Casualty Co. v. First Nat. Bank*, 246 Fed. 892; *Illinois Surety Co. v. Donaldson*, 202 Ala. 183, 79 So. 667; *State Camp v. Kelley*, — Pa. —, 110 Atl. 339.

Construction of fidelity bond, see *Illinois Surety Co. v. Donaldson*, 202 Ala. 183, 79 So. 667.

Sufficiency of complaint in action on fidelity bond of embezzling cashier of bank, see *Union Nat. Bank v. United States Fidelity & Guaranty Co.*, 143 La. 329, 78 So. 582.

⁴¹ *First Nat. Bank v. National Surety Co.*, 228 N. Y. 469, 127 N. E. 479, rev'g 182 N. Y. App. Div. 262, 169 N. Y. Supp. 774.

⁴² What constitutes “willfully misapplied or willfully ab-

stracted,” within meaning of cashier's bond, see *National Surety Co. v. Atascosa Ice, Water & Light Co.*, — Tex. Civ. App. —, 222 S. W. 597.

Bond of cashier, liability of surety company on, see *Eland State Bank v. Massachusetts Bonding & Insurance Co.*, 165 Wis. 493, 162 N. W. 662.

Surety bonds, liability for loan made to president, see *American Surety Co. v. State ex rel. Booth*, — Ind. App. —, 127 N. E. 844.

⁴³ *Green v. Interstate Casualty Co.*, 256 Fed. 81.

⁴⁴ *United States Fidelity & Guaranty Co. v. Walker*, 248 Fed. 42.

⁴⁵ *Webster v. Jossman*, 199 Mich. 98, 165 N. W. 802.

office is indefinite or during the pleasure of the appointing power, and the obligation of the surety is couched in general language, the surety contracts for such indefinite term or during the pleasure of the appointing power.⁴⁶

V. TERM OF OFFICE

§ 1799. General rules. The fact that by-laws provide that the treasurer should be elected each year, and forbid his removal with or without cause by the directors, does not affect the power of the corporation to contract with an incorporator for his employment as treasurer for a definite term.⁴⁷

§ 1800. During pleasure of board of directors.⁴⁸ Where a statute fixes a cashier's term of office as at the pleasure of the directors, it cannot be changed to an annual one by a by-law.⁴⁹ The Washington statute giving corporations power to remove their officers, agents and servants "at will" makes any contract of employment by a corporation void and unenforceable so far as it is a contract for a fixed time.⁵⁰ Since cashiers of national banks hold their office subject to dismissal at the pleasure of the board of directors, a cashier employed for a year cannot sue because of his discharge without cause before the end of the year.⁵¹

§ 1806. Effect of disposing of stock after election, so as to disqualify officer.⁵² A by-law that "when one ceases to be a stockholder his office as a director shall become vacant" makes the office ipso facto vacant upon a sale of the stock; and a director ceases to be a director on the sale of his stock although he continues to be the registered holder thereof.⁵³ If a director,

⁴⁶ Webster v. Jossman, 199 Mich. 98, 165 N. W. 802.

⁴⁷ Reiss v. Usona Shirt Co., 174 N. Y. App. Div. 181, 159 N. Y. Supp. 1031.

⁴⁸ Acts of directors held to constitute a re-election of secretary for two years, and that the phrase "subject to the will of the board of directors" referred to his compensation and not his term of office, see Barker v. National Life

Ass'n, 183 Iowa 966, 166 N. W. 597.

⁴⁹ Webster v. Jossman, 199 Mich. 98, 165 N. W. 802.

⁵⁰ Williams v. Great Northern R. Co., 108 Wash. 344, 184 Pac. 340.

⁵¹ First Nat. Bank v. Miller, 23 Ga. App. 441, 98 S. E. 402.

⁵² See also § 1777, *supra*.

⁵³ Johnson v. York Coal & Coke Co., 182 Ky. 303, 206 S. W. 611.

after election, reassigns his one share of stock assigned to him to qualify him, it seems that he ceases to be a director.⁵⁴

§ 1808. Holding over. A holdover officer need not be formally re-elected, but it is sufficient that the directors fix his salary for the succeeding year.⁵⁵ Where the term of office is for two years and until a successor is elected, failure to hold a meeting to elect a successor at the regular time does not entitle a holdover officer to another two-year term.⁵⁶

VI. RESIGNATION

§ 1813. Effect of resignation. Resignation of the treasurer not only terminates his authority but also any authority delegated by him to others.⁵⁷ While, in the absence of statutory regulations there are cases which hold that the resignation of a corporate officer takes effect on his delivery to the proper officer of his written resignation and before acceptance thereof by the board of directors, these are generally cases where some remedy is sought against the director personally, and their basis is that where a director or officer thus resigns, the inaction or refusal of a board of directors should not impose upon him a future liability or responsibility which he does not desire to undertake. There are also cases where an officer or director of a foreign corporation, who intends to visit another jurisdiction, may resign in order to avoid service of a summons in a foreign jurisdiction. But where resignations of officers or directors are attempted in order to effectuate a fraud, as where a director resigns as part of a fraudulent scheme to prevent service on him of an order for examination in supplementary proceedings and thereby to prevent collection of a judgment, the resignation is not effective as against the judgment creditor regardless of its effect as between the director and the corporation.⁵⁸

⁵⁴ *Snyder v. Bender*, 173 N. Y. Supp. 401.

⁵⁵ *Hess v. Kismet State Bank*, 106 Kan. 701, 189 Pac. 919.

⁵⁶ *Barker v. National Life Ass'n*, 183 Iowa 966, 166 N. W. 597.

⁵⁷ *Emerson v. Fisher*, 246 Fed. 642.

⁵⁸ *Inventions Corporation v. Hobbs*, 244 Fed. 430, 442, 443.

VII. REMOVAL OF OFFICERS

§ 1814. Inherent power—In general. A director cannot be suspended or removed from office until the end of his term, at least without cause.⁵⁹ Directors cannot remove an officer, except for cause, where elected for a specified term.⁶⁰

§ 1817. Express power—In general. A by-law giving directors arbitrary power to remove the general manager or any officer or employee is within the power of a farmer's co-operative corporation.⁶¹

§ 1819. Who may remove. An officer elected by the board of directors and subject to removal by it is not subject to discharge by the general manager.⁶²

§ 1820. Resort to courts to obtain removal—In general. It seems that, in an action by stockholders, a court may remove the president of a corporation from his office as director on an allegation that he draws an exorbitant salary of ten thousand dollars a year which is a wasteful expenditure.⁶³

§ 1821. — Who may sue. An executor to whom two shares of stock are left for purposes of deciding disputes between the two other stockholders has no such individual interest as to entitle him to proceed to set aside an election of directors.⁶⁴

§ 1822. Resort to courts to interfere with action of corporate officers in regard thereto. Equity cannot reinstate a corporate officer who claims he has been wrongfully discharged.⁶⁵ A minority director has no legal grievance on account of his removal from office.⁶⁶

⁵⁹ Walsh v. State ex rel. Cook, 199 Ala. 486, 74 So. 45.

⁶⁰ Barker v. National Life Ass'n, 183 Iowa 966, 166 N. W. 597.

⁶¹ Rundell v. Farmers' Co-Op. Elevator Co. of Corunna, 210 Mich. 642, 178 N. W. 21.

⁶² Birmingham Realty Co. v. Hale, 16 Ala. App. 460, 78 So. 723.

⁶³ State ex rel. Smalley v. Reyn-

olds, 275 Mo. 113, 204 S. W. 1093.

⁶⁴ In re P. F. Keogh, Inc., 192 N. Y. App. Div. 624, 183 N. Y. Supp. 408.

⁶⁵ Cuppy v. Ward, 187 N. Y. App. Div. 625, 176 N. Y. Supp. 233.

⁶⁶ Kavanaugh v. Kavanaugh Knitting Co., 184 N. Y. App. Div. 650, 172 N. Y. Supp. 576.

VIII. REMEDIES TO DETERMINE TITLE TO OFFICE

§ 1826. Quo warranto.⁶⁷§ 1828. Jurisdiction in equity—General rule.⁶⁸§ 1829. — Exceptions to rule.⁶⁹§ 1830. Statutory remedies.⁷⁰

§ 1832. **Collateral attack.** The right of corporate officers to hold office cannot be attacked collaterally.⁷¹ The legality of an election of corporate officers not attacked in the home state cannot be attacked a considerable time thereafter in a foreign state in connection with a settlement in bankruptcy proceedings.⁷²

IX. DE FACTO OFFICERS

§ 1833. **General considerations.** There need not be a de jure officer in order for there to be a de facto one.⁷³ There may be a de facto private office, such as subordinate offices of private corporations, although there cannot be a de facto public office.⁷⁴

§ 1835. **To what officers applicable—Necessity for color of title.** A person elected by the directors and held out to the public for several years as assistant cashier of a bank is a de facto if not a de jure officer of the bank.⁷⁵

§ 1840. **De jure office as essential to de facto officer.** However, in a criminal prosecution for embezzlement the existence of a de jure office need not be proven by a by-law duly adopted by the stockholders.⁷⁶

⁶⁷ See § 1699, *supra*.⁶⁸ See § 1700, *supra*.⁶⁹ See § 1700, *supra*.⁷⁰ See § 1704, *supra*.⁷¹ *Cabana v. Holstein-Friesian Ass'n of America*, — N. Y. Misc. —, 182 N. Y. Supp. 658.⁷² *In re O'Gara Coal Co.*, 260 Fed. 742.⁷³ *Ex parte State*, 201 Ala. 59,77 So. 353, *rev'g Kramer v. State*, 16 Ala. App. 40, 75 So. 185.⁷⁴ *Ex parte State*, 201 Ala. 59, 77 So. 353, *rev'g Kramer v. State*, 16 Ala. App. 40, 75 So. 185.⁷⁵ *Ex parte State*, 201 Ala. 59, 77 So. 353, *rev'g Kramer v. State*, 16 Ala. App. 40, 75 So. 185.⁷⁶ *Ex parte State*, 201 Ala. 59, 77 So. 353, *rev'g on this ground*

Ch. 42] DIRECTORS, OTHER OFFICERS AND AGENTS [§ 1854

§ 1841. Powers and rights of de facto officers—In general. A conveyance by de facto officers is valid.⁷⁷

§ 1846. Acts as binding in favor of third persons—General rules. A corporation is bound by the acts of de facto officers in dealings with third persons who have no knowledge of any want of power on the part of the officers.⁷⁸

§ 1851. Collateral attack by third persons. The acts of de facto officers cannot be collaterally attacked.⁷⁹

§ 1852. Liabilities of de facto officers. An assistant cashier who has acted as such for years is estopped to deny there was such de jure office and that he was such de jure or de facto officer, in a prosecution for embezzlement.⁸⁰

X. MEETINGS OF DIRECTORS

§ 1853. General considerations. Motive of directors in adopting resolutions are of no effect in the courts, since "if the legality of the act of a director of a corporation depended upon the motive which actuated him, every act of the directory might be questioned."⁸¹

§ 1854. Necessity for action as a board—In general. Directors cannot contract except when acting as a body.⁸² Trustees of a religious corporation cannot bind it separately but only as a board.⁸³ Directors, by agreement among themselves other

Kramer v. State, 16 Ala. App. 40, 75 So. 185, which is set forth in the note on pp. 3034, 3035, Fletcher Cyc. Corp.

⁷⁷ See Neptune Mildew & Waterproofing Co. v. Central R. Co., — N. J. Eq. —, 102 Atl. 442.

⁷⁸ Rhea v. Newton, 262 Fed. 345; Arney v. Brittain & Co., 185 Iowa 1114, 171 N. W. 697; Traders Trust Co. v. Goodman, 37 Dom. L. Rep. (Can.) 31.

⁷⁹ Guaranty Loan Co. v. Fontanel, — Cal. —, 190 Pac. 177; Ellsworth v. National Home &

Town Builders, 33 Cal. App. 1, 164 Pac. 14.

⁸⁰ Ex parte State, 201 Ala. 59, 77 So. 353, rev'g Kramer v. State, 16 Ala. App. 40, 75 So. 185.

⁸¹ Haldeman v. Haldeman, 176 Ky. 635, 197 S. W. 376.

⁸² Caddy Oil Co. v. Sommer, 186 Ky. 843, 218 S. W. 288.

⁸³ Parucki v. Polish Nat. Catholic Church of Holy Mother of Rosary, — N. Y. Misc. —, 177 N. Y. Supp. 206.

than at a directors' meeting, cannot agree with the president to pay him a specified sum out of the corporate funds when nothing was due him.⁸⁴

§ 1855. — Effect of consent of all of directors. Consent of directors separately obtained and not given in a board meeting is not equivalent to formal action of the board.⁸⁵ Consent of a majority of the directors, although not at a formal meeting, is sufficient where acquiesced in by all the stockholders and other directors for a long period of time.⁸⁶

§ 1856. — Exception where custom or usage to the contrary. Formal meetings of directors are not necessary where their usual course of business is to act informally.⁸⁷

§ 1862. Time of meetings—In general. A meeting of directors called for ten a.m. is valid although the directors do not assemble until one p.m., in the absence of special circumstances.⁸⁸

§ 1863. — Adjournments. Notice of an adjourned directors' meeting need not be given.⁸⁹

§ 1865. Place of meeting—Outside the state. Where the certificate of incorporation provides that directors' meetings may be held outside the state, such meetings outside the state are proper in Delaware although no by-law provides therefor and another statute authorizes meetings outside the state if the by-laws so provide.⁹⁰ The informality of a meeting held outside the state may be waived by the stockholders and the act ratified by their subsequent consent and acquiescence.⁹¹

⁸⁴ Moss v. Copelof, 231 Mass. 513, 121 N. E. 508.

⁸⁵ Coleman v. Northwestern Mut. Life Ins. Co., 273 Mo. 620, 201 S. W. 544.

⁸⁶ Gorrill v. Greenlees, 104 Kan. 693, 180 Pac. 798.

⁸⁷ Baker v. Smith, 41 R. I. 17, 102 Atl. 721.

⁸⁸ Whitecomb v. Giannini, — Cal. App. —, 184 Pac. 887.

⁸⁹ Whitecomb v. Giannini, — Cal. App. —, 184 Pac. 887.

⁹⁰ Lippman v. Kehoe Stenograph Co., — Del. —, 102 Atl. 988.

⁹¹ In re Wilson's Estate, 85 Ore. 604, 67 Pac. 580.

§ 1868. Necessity for notice of meetings—Special meetings. The statutory requirement of special notice to each director of special meetings is not affected by the fact that the directors actually have knowledge of the time and place of such a meeting.⁹² It "is a serious question whether, if a majority be present, its action is ever invalidated because there was a failure to give notice of the meeting to one who, if notified and present, would be sure to be opposed to any action of the majority because such action might be injurious to him personally."⁹³

§ 1875. — To whom notice must be given. Of course notice of a directors' meeting need not be given to persons who have ceased to be directors because of the sale of their stock.⁹⁴

§ 1882. Quorum—What is in absence of regulatory provision. A directors' meeting is invalid where there is not a quorum present.⁹⁵ A resolution reducing the number of directors necessary to constitute a quorum, merely to enable another resolution to be passed conferring an interest in the property of the company on a director whose vote could not be counted to constitute a quorum, is invalid as an attempt to do indirectly what could not be done directly.⁹⁶

§ 1889. Counting interested or disqualified directors. A director disqualified because of interest cannot vote,⁹⁷ and cannot be counted to ascertain whether a quorum is present.⁹⁸ If the vote of an interested director is necessary for a majority, the vote is invalid.⁹⁹ But the vote of an interested director does not invalidate a resolution where adopted by a disinterested majority.¹ Where the charter forbids directors to vote in respect to any contract with themselves, the issue of two debentures to

⁹² Beatty v. Rianda, 34 Cal. App. 180, 167 Pac. 185.

⁹³ Ney v. Eastern Iowa Tel. Co., 185 Iowa 610, 171 N. W. 26.

⁹⁴ Johnson v. York Coal & Coke Co., 182 Ky. 303, 206 S. W. 611.

⁹⁵ Engles v. Shaffer, — Ark. —, 219 S. W. 343.

⁹⁶ In re North Eastern Ins. Co., Ltd., [1919] 1 Ch. Div. 198.

⁹⁷ Fields v. Victor Building &

Loan Co., — Okla. —, 175 Pac. 529.

⁹⁸ Fields v. Victor Building & Loan Co., — Okla. —, 175 Pac. 529.

⁹⁹ Nordgren v. Oldham Rural Tel. Co., 40 S. D. 460, 168 N. W. 26.

¹ In re Franklin Brewing Co., 263 Fed. 512.

two directors, where forming part of one transaction in which both were equally interested, is invalid where the two directors had to be counted to constitute a quorum.² But a wife is not disqualified from voting at a directors' meeting in fixing the sum to which her husband was entitled as manager under his written contract, the construction of which was in dispute.³

§ 1891. Presumptions in favor of meeting. Notice of a directors' meeting, where necessary, will be presumed to have been given, in the absence of a showing to the contrary.⁴ One who attacks the validity of a directors' meeting on the ground of want of notice has the burden of proving it.⁵

§ 1892. Effect of irregularity or illegality—In general. The failure to make proper minutes of a directors' meeting does not invalidate authority conferred at such a meeting.⁶

§ 1893. — Ratification by directors or stockholders. Stockholders who knowingly have for over two years recognized the validity of directors' meetings without notice to an absent director who in fact never acted as director, cannot assert that such meetings were illegal for failure to give such notice.⁷ The purchasers of stock from certain directors cannot assert the illegality of the directors' meeting authorizing the issuance of such stock, where the selling directors voted for the resolution authorizing such issuance, since the purchasers stand in the shoes of the selling directors.⁸ Failure to give notice of a directors' meeting at which a sale by an agent of all the corporate effects was agreed on cannot be raised by a director not notified or present, some three years thereafter, where no director had objected in the meantime during which the stockholders had without objection received about two-thirds of the purchase price.⁹

² *In re North Eastern Ins. Co., Ltd.*, [1919] 1 Ch. Div. 198.

³ *Cuneo v. Giannini*, — Cal. App. —, 180 Pac. 633.

⁴ *Whitcomb v. Giannini*, — Cal. App. —, 184 Pac. 887.

⁵ *La Habra Oil Co. v. Francis*, 35 Cal. App. 168, 169 Pac. 401.

⁶ *Engles v. Shaffer*, — Ark. —, 219 S. W. 343.

⁷ *Berman v. Minneapolis Photo Engraving Co.*, 144 Minn. 146, 174 N. W. 735.

⁸ *Berman v. Minneapolis Photo Engraving Co.*, 144 Minn. 146, 174 N. W. 735.

⁹ *Gorrill v. Greenlees*, 104 Kan. 693, 180 Pac. 798.

Ch. 42] DIRECTORS, OTHER OFFICERS AND AGENTS [§ 1900

§ 1895. Vote or resolution as constituting a contract. A resolution of a board of directors may constitute a contract.¹⁰

XI. POWERS OF OFFICERS AND AGENTS IN GENERAL

§ 1896. General rules. The fact that a corporate officer pays all the corporate debts does not give him any added authority to act for the corporation.¹¹ A corporate officer cannot make the corporation liable for the debt of another by merely stating an account with the creditor.¹² Title to negotiable instruments is not changed by unauthorized indorsements by officers having no authority to indorse.¹³

§ 1897. Rules of agency as applicable. The status of a person as an agent is not affected by the fact that he is acting for a corporation rather than an individual.¹⁴ The power of corporate officers and agents to bind the corporation is governed by the general law of agency, the underlying principles being the same.¹⁵

§ 1899. Classification and enumeration of powers—Powers expressly conferred. Authority conferred on an officer to sell a right of way does not authorize a sale of the fee.¹⁶ A vote of members of a church may authorize an officer to make a contract although it could not be consummated without the written consent of a majority of the members.¹⁷

§ 1900. — Powers incidental to express powers conferred.¹⁸ Power of a corporate officer to contract includes power to fix the

¹⁰ Schlens v. Poe, 128 Md. 352, 97 Atl. 649.

¹¹ Burgess Battery Co. v. Solar Light Co., 266 Fed. 368.

¹² Patterson, Gottfried & Hunter v. Levy, — N. Y. Misc. —, 177 N. Y. Supp. 895.

¹³ Emerson v. Fisher, 246 Fed. 642.

¹⁴ Bright v. Virginia & Gold Hill Water Co., 254 Fed. 175.

¹⁵ Rae v. Heilig Theatre Co., 94 Ore. 408, 185 Pac. 909.

¹⁶ Louisiana Sulphur Min. Co. v. Brimstone Railroad & Canal Co., 143 La. 743, 79 So. 324.

¹⁷ Stablein v. Hutterische Gemeinde, — S. D. —, 177 N. W. 810.

¹⁸ Authority of officers to sign petitions for public improvements, see Walton v. Commissioners of Light Improvement Dist. No. 1, City of Benton, — Ark. —, 222 S. W. 1056.

Account stated, powers of cor-

price.¹⁹ On the other hand, authority to sell for cash carries no authority to sell for less than cash.²⁰

§ 1901. — Inherent powers or powers arising merely by virtue of the office. Only the directors can transfer all the corporate property as security for a debt.²¹

§ 1904. How authority conferred. The officer's or agent's authority need not be evidenced by an express writing,²² nor by entries in the corporate books,²³ nor by a resolution or other express declaration by the directors, but it may be proven by circumstantial evidence.²⁴ Parol evidence is admissible to show authority of corporate officers where no records of the directors' meetings have been made or they have been lost.²⁵ Recitals in a deed of trust executed by a corporation, relating to the adoption of resolutions of stockholders and directors, may be relied on by persons dealing with the corporation without notice, since such corporate records are private records and need not be further inquired into.²⁶

porate officers to make and render, see part of note in 2 A. L. R. 71, on pages 77-79.

¹⁹ *The Allen Wilde*, 264 Fed. 291.

²⁰ *Empire Coal Min. Co. v. Empire Coal Co.*, 183 Ky. 699, 210 S. W. 474.

²¹ *Snyder v. Bender*, 173 N. Y. Supp. 401.

²² *Alabama City, G. & A. R. Co. v. Kyle*, 202 Ala. 552, 81 So. 54, and see § 1767, *supra*.

In the absence of any charter prohibition, a vote of a corporation to confer authority on an agent to convey personal property and execute the conveyance need not be in writing. *Alabama City, G. & A. R. Co. v. Kyle*, 202 Ala. 552, 81 So. 54.

As to applicability to corporate officers and employees of statute requiring agent's authority to be in writing, see also note in 1 A.

L. R. 1132, annotating *McCartney v. Clover Valley Land & Stock Co.*, 232 Fed. 697, 1 A. L. R. 1127.

²³ *Cyclops Iron Works v. Chico Ice & Cold Storage Co.*, 34 Cal. App. 10, 166 Pac. 821.

²⁴ *E. Aigeltinger, Inc. v. Burke*, 176 Cal. 621, 169 Pac. 373.

Authority of an agent may be proved by evidence that he does business for the corporation with the knowledge and acquiescence of its directors or general manager or by their direction. Proof by the minutes of the board or by a written contract is not necessary. *City of Venice v. Short Line Beach Land Co.*, — Cal. —, 181 Pac. 658.

²⁵ *Fowler Gas Co. v. Weber*, — Cal. —, 181 Pac. 663; *Abo Land Co. v. Dunlavy*, — N. M. —, 181 Pac. 582.

²⁶ *Hartley v. Ault Woodenware Co.*, 82 W. Va. 780, 97 S. E. 137.

§ 1905. Statements of officer or agent as to his powers. Corporate agency cannot be proved as against third persons by the declarations of the agent.²⁷ Neither the declarations of an alleged general manager "nor of any other person in the office, with regard to his authority to represent the defendant, are binding on it or have any probative force on the issue with respect to his agency."²⁸

§ 1910. Ultra vires acts—General rules. An officer of a bank cannot bind the bank by an ultra vires accommodation indorsement or guaranty.²⁹

§ 1916. Apparent power and estoppel to deny power—General rules. A corporation is bound by the acts of its officers and agents within the scope of their apparent authority.³⁰ Actual authority conferred on corporate agents is immaterial where the question is as to their apparent or ostensible authority.³¹ Apparent authority cannot be defeated by failure to enter on the directors' minutes any order giving authority to act.³²

§ 1918. — What constitutes apparent authority. The term "apparent authority" is technical and should be defined by

²⁷ *Oklahoma Automobile Co. v. Benner*, — Okla. —, 174 Pac. 567. Contra, see *Pacific Power & Light Co. v. White*, 104 Wash. 528, 177 Pac. 313.

²⁸ *Loeb v. Star & Herald Co.*, 187 N. Y. App. Div. 175, 175 N. Y. Supp. 412.

²⁹ *Wagner v. Central Banking & Security Co.*, 249 Fed. 145.

³⁰ *Newton v. Johnston Organ & Piano Mfg. Co.*, — Cal. —, 180 Pac. 7; *Commercial Security Co. v. Modesto Drug Co.*, — Cal. App. —, 184 Pac. 964; *Hammit v. Virginia Min. Co.*, 32 Idaho 245, 181 Pac. 336; *Sternberger v. Anheuser-Busch Brewing Ass'n*, 203 Ill. App. 86; *Caddy Oil Co. v. Sommer*, 186 Ky. 843, 218 S. W. 288; *Com. v. Mehler & Eckstenkemper*

Lumber Co., 183 Ky. 11, 208 S. W. 13; *Penick & Ford v. C. La. garde & Co.*, 146 La. 511, 83 So. 787; *Willson v. Chicago Bonding & Surety Co.*, — Mo. —, 214 S. W. 371; *Magnolia Compress & Warehouse Co. v. St. Louis Cash Register Co.*, 201 Mo. App. 201, 210 S. W. 125; *Sapulpa Co. v. State ex rel. Lankford*, — Okla. —, 166 Pac. 119; *F. L. Shaw Co. v. Dalton Adding Mach. Co.*, — Tex. Civ. App. —, 211 S. W. 833; *Hartley v. Ault Woodenware Co.*, 82 W. Va. 780, 97 S. E. 137.

³¹ *Newton v. Johnston Organ & Piano Mfg. Co.*, — Cal. —, 180 Pac. 7.

³² *Fowler Gas Co. v. Weber*, — Cal. —, 181 Pac. 663.

the court in its instructions, where requested.³³ An isolated act does not confer ostensible authority.³⁴ Ostensible authority of a general manager to guarantee an account is shown by the fact that such guaranties executed for a long period of time were never questioned by the board of directors and that the bills guaranteed were always paid.³⁵ The continued exercise by the treasurer of a corporation of the power to execute notes with the apparent acquiescence of the board of directors estops the corporation from questioning his authority.³⁶ Where the vice president is held out by the corporation as its agent or officer to execute notes and contracts, the corporation is estopped to deny his authority so to do.³⁷

The rule that the apparent scope of an agent's authority is necessarily limited by the usage and practice obtaining in the conduct of the particular line of business in which he is employed applies equally well both to the chief executive officer of a corporation and a mere traveling salesman.³⁸

§ 1920. — Application of rule to abuse of apparent authority. A person dealing with a corporation cannot be held responsible for a subsequent conversion of money, bonds or the like paid or delivered to the officer of the corporation conducting the negotiations.³⁹

§ 1922. — As affected by secret instructions or prohibitions. Apparent authority cannot be limited by secret instructions.⁴⁰ For instance, authority of the president cannot be controlled by secret restrictions and agreements among the stockholders.⁴¹ So legal title to notes payable to a corporation passes

³³ *Emerson-Brantingham Implement Co. v. Roquemore*, — Tex. Civ. App. —, 214 S. W. 679.

³⁴ *First State Bank v. Lang*, 55 Mont. 146, 9 A. L. R. 1139, 174 Pac. 597.

³⁵ *Armour & Co. v. R. Rosenberg & Sons Co.*, 36 Cal. App. 773, 173 Pac. 404.

³⁶ *Quinn v. Quinn Mfg. Co.*, 201 Mich. 664, 167 N. W. 898.

³⁷ *Alabama City, G. & A. R. Co. v. Kyle*, 202 Ala. 552, 81 So. 54.

³⁸ *Continental Ins. Co. v. Schulman*, 140 Tenn. 481, 205 S. W. 315.

³⁹ *Mitchell Street State Bank v. Schaefer*, 168 Wis. 543, 173 N. W. 330.

⁴⁰ *Empire Coal Min. Co. v. Empire Coal Co.*, 183 Ky. 699, 210 S. W. 474.

⁴¹ *Phillips v. Interstate Land Co.*, 176 N. C. 514, 97 S. E. 417.

to a stockholder on their being indorsed by the president of the company, notwithstanding a resolution of the directors limiting the powers of the president.⁴² A resolution of a board of directors is not binding on one dealing with the corporation where he had no knowledge thereof before the contract was closed.⁴³

§ 1927. Actual or constructive notice of powers of officers or agents to third persons dealing with corporation—Actual notice. A conveyance of certain property by the president and treasurer is limited in its scope to the special authority conferred by the directors on such officers to make the transfer, where the transferee had knowledge of such limited authority.⁴⁴ If one loaning money to a corporation through its president has notice that in reality the loan was for the personal use of the president, the lender cannot hold the corporation liable.⁴⁵

§ 1928. — Constructive notice. A transfer of negotiable paper by a bank cashier, plainly out of the usual course of business of the bank, is not binding on the bank even though the transferee paid value, where he must have known the cashier was acting outside the scope of his duties.⁴⁶

§ 1929. — Notice from individual or adverse interest of officer or agent. Where, in a particular transaction, knowledge is brought to a person dealing with a corporation that its officer or agent conducting the deal has an interest adverse to that of the corporation, it is sufficient to put him on notice of want of authority to bind the corporation.⁴⁷ Stated in another way,

⁴² *Cardwell v. Garrison*, 179 N. C. 476, 103 S. E. 3.

⁴³ *Minneapolis Holding Co. v. Landers-Morrison-Christenson Co.*, 141 Minn. 127, 169 N. W. 534.

⁴⁴ *Vreeland v. Irving*, — Conn. —, 99 Atl. 574.

⁴⁵ *Gross Iron Ore Co. v. Paulle*, 143 Minn. 48, 172 N. W. 907.

⁴⁶ *Choctaw Bank v. Gewin*, 16 Ala. App. 349, 78 So. 96.

⁴⁷ *Wagner v. Central Banking & Security Co.*, 249 Fed. 145; *First*

Nat. Bank v. Drovers' & Mechanics' Nat. Bank, 244 Fed. 135; *Harwood v. Ft. Worth Nat. Bank*, — Tex. Civ. App. —, 205 S. W. 484.

Where corporate funds were used by the president to pay his individual debt to a stockholder, the latter is liable to the corporation or its trustee in bankruptcy for money had and received to the extent of the amount so paid, where he received the money with knowl-

a party dealing with a corporate officer, knowing him to be acting in his own interest, takes the risk of his having authority to act for the corporation, and assumes the burden of establishing such authority when he seeks to hold the corporation.⁴⁸ The rule of apparent authority is confined to cases where the officer or agent is not known by the other party to be acting in his own interest instead of the interest of the corporation, or where the circumstances are not such that the other party is chargeable with knowledge that the official is acting in his own interest.⁴⁹

The most usual application of this rule is in case of corporate paper made out to or indorsed by a corporate officer and turned over by him in payment of or as security for a personal debt, in which case the other party is bound to take notice of the want of authority of the officer to do the particular act.⁵⁰ Notes,⁵¹

edge that it was corporate funds. *Walton v. Chalmers*, — Mo. App. —, 205 S. W. 90.

⁴⁸ *First Nat. Bank v. Rust*, 257 Fed. 29.

⁴⁹ *First Nat. Bank v. Rust*, 257 Fed. 29, applying limitation to issuance of certificate of deposit by bank president on payment of his individual debt.

⁵⁰ *McDowell v. Bauman*, 189 Ky. 136, 224 S. W. 641; *McCullam v. Buckingham Hotel Co.*, 198 Mo. App. 107, 199 S. W. 417; *J. B. Kepner Co. v. Hutton*, 179 N. Y. App. Div. 130, 166 N. Y. Supp. 408; *Martindale v. DeKay*, 101 N. Y. Misc. 728, 166 N. Y. Supp. 405.

In Missouri, in 1917, a statute was enacted protecting the person taking such paper from a corporate officer or agent unless taken with actual knowledge of the want of authority of the officer or agent, and this statute was held not retroactive. *McCullam v. Buckingham Hotel Co.*, 198 Mo. App. 107, 199 S. W. 417.

For note on "Right of one who takes commercial paper of cor-

poration in payment of or security for an individual debt of an officer," see L. R. A. 1918 F 1163, annotating *Burnham Loan & Investment Co. v. Sethman*, — Colo. —, L. R. A. 1918 F 1158, 171 Pac. 884.

⁵¹ One who receives from the president of a corporation a note of the corporation in exchange for a personal note of such president does so at his peril and will be deemed to have taken with notice of the want of authority to deliver the corporate note for such purpose. *Hoffman v. M. Gottstein Inv. Co.*, 101 Wash. 428, 172 Pac. 573.

Where a note is indorsed for transfer by a corporate officer in the corporate name, and given as collateral for a loan to himself individually or to some other corporation in which he is interested, the transferee is put on inquiry as to the actual authority of the officer to make the transfer. *Bank of Benson v. Gordon*, 103 Neb. 508, 172 N. W. 367.

checks,⁵² drafts,⁵³ and certificates of deposits,⁵⁴ are all within the rule. But the rule that checks drawn by a corporate officer on his company for his individual use are invalid does not apply where an officer was allowed for years to draw company checks for his salary and indorse them to others in payment of his debts.⁵⁵ Likewise, while a person who takes the note of a corporation in payment of the personal obligation of its officers is

⁵² One accepting a check of a corporation drawn by an officer thereof in payment of his private obligations takes the risk of want of authority to use the check for a private purpose. *O'Bannon v. Moerschel*, — Mo. App. —, 222 S. W. 1035, which rule, however, is modified by a Missouri statute enacted in 1917; *McCullam v. Mermod, Jaccard & King Jewelry Co.*, — Mo. App. —, 218 S. W. 345; *Napoleon Hill Cotton Co. v. Stix, Baer & Fuller Dry Goods Co.*, — Mo. App. —, 217 S. W. 323; *Reynolds v. Union Station Bank of St. Louis*, 198 Mo. App. 323, 200 S. W. 711.

Payments of individual debts by an officer by checks drawn directly on the corporation are presumptively unauthorized. *Atherton v. Beaman*, 256 Fed. 871.

A corporation may recover its money paid to a creditor of its officer by a corporate check payable to the officer, although the directors consented to the payment, where the consent was given under the mistaken idea that the debt paid was a corporate debt. *O'Bannon v. Moerschel*, — Mo. App. —, 222 S. W. 1035.

It is the duty of a bank to inquire as to the authority of the secretary of a corporation to indorse a check payable to the corporation, presented by him for deposit in his individual account,

where there has been no previous course of dealing; and the corporation may recover the amount from the bank where the secretary had no such authority. *Buena Vista Oil Co. v. Park Bank*, 39 Cal. App. 710, 180 Pac. 12. But where a corporation gave its secretary power to indorse in blank checks payable to the corporation, it has been held that title passes on delivery to a bank for deposit to the credit of his own account unless the bank had notice of want of title or acted in bad faith. *Santa Marina Co. v. Canadian Bank of Commerce*, 254 Fed. 391.

⁵³ If drafts drawn in the name of a savings bank are used by a national bank in discharge of the individual liability of the president of the savings bank to it, the national bank is chargeable with notice of the want of power of the president to so use the drafts. *Harwood v. Ft. Worth Nat. Bank*, — Tex. Civ. App. —, 205 S. W. 484.

⁵⁴ A bank president giving a certificate of deposit in payment of his individual debt, the creditor is chargeable with notice of his want of authority. *First Nat. Bank of Sweetwater, Texas v. Rust*, 257 Fed. 29.

⁵⁵ *Napoleon Hill Cotton Co. v. H. Oetter Grocery Co.*, — Mo. App. —, 222 S. W. 876.

put upon inquiry as to the authority of the officer, the note is not void but only voidable at the instance of the corporation.⁵⁶ And in one case it was held that where the secretary of a corporation indorses checks for transfer and deposits them in his individual account, the bank has a good title unless it has notice that the secretary had no title to them or there was some act of bad faith on the part of the bank in receiving the checks; and where the corporation gave the secretary authority to indorse checks without restriction, it was estopped to obtain the amount from the bank in which the secretary deposited them in his individual account, where the bank acted in good faith.⁵⁷

§ 1931. — By-laws as notice. By-laws are sometimes admissible to show the limitations of the authority of a corporate officer or agent.⁵⁸ But a by-law limiting the powers of a corporate officer has no effect, as against one not a member of the corporation, to preclude him relying on the apparent authority conferred on the officer.⁵⁹

§ 1932. Constructive notice of powers of officers or agents by members or other officers of corporation. Whatever ostensible authority an officer has in dealing with strangers, he has only such authority in dealing with a director as is conferred on him by virtue of his office or by express grant from the board of directors.⁶⁰

§ 1934. Power to execute commercial paper. Authority to purchase generally includes power to execute a note for the purchase price.⁶¹

⁵⁶ *Norment v. First Nat. Bank*, — N. M. —, 167 Pac. 731.

⁵⁷ *Santa Marina Co. v. Canadian Bank of Commerce*, 254 Fed. 391.

⁵⁸ *St. Louis Beverage Co. v. Planters' Grain Elevator, Mule & Feed Co.*, — Mo. App. —, 200 S. W. 780; *McAllister v. Pittsburgh Water Heater Co.*, 65 Pa. Super. Ct. 522.

⁵⁹ *Hartford v. Massachusetts Bowling Alleys*, 229 Mass. 30, 118 N. E. 188; *Shpunt v. Machinery Merchants*, 112 N. Y. Misc. 457, 183 N. Y. Supp. 90; *Spitzer v.*

Born, 111 N. Y. Misc. 595, 182 N. Y. Supp. 327.

⁶⁰ *First State Bank v. Lang*, 55 Mont. 146, 9 A. L. R. 1139, 174 Pac. 597.

A bank cashier, in dealing with a director, has no apparent authority greater than his inherent or expressly delegated authority. *First State Bank v. Lang*, 55 Mont. 146, 9 A. L. R. 1139, 174 Pac. 597.

⁶¹ *Swift & Co. v. Dawson Paper Shell Pecan Co.*, — Ga. App. —, 101 S. E. 754.

§ 1937. Power to employ physicians and surgeons.⁶² An assistant engineer of a railroad company has no power to hire a physician to attend to injuries to servants where injured while not at work.⁶³

§ 1939. Powers of subordinate agents or employees.⁶⁴ "There is no presumption that bookkeepers or assistant treasurers or cashiers may by any act of their own, and merely because they know the rights of the employer have been invaded, release the wrongdoer from the liability created by such invasion."⁶⁵ A station agent has no authority to contract for board of an animal injured during shipment.⁶⁶ The position of a "receiving and paying teller" in a bank is distinctly recognized as to character and functions.⁶⁷

§ 1940. — Powers of purchasing or selling agents. A sales agent has no power to modify a contract of the corporation.⁶⁸

§ 1941. Powers of general solicitor or counsel, and of attorneys. A claims attorney, not an executive or administrative officer of the corporation, cannot verify an application for a change of venue.⁶⁹

§ 1942. When powers terminate. Delegated authority ceases upon the resignation of the officer who delegated such authority.⁷⁰

⁶² Note on "Implied authority of officers, agents, or servants to contract for medical, surgical, or other attendance or supplies for sick or injured persons," see Ann. Cas. 1918 A 791.

⁶³ *Carson v. Chicago, M. & St. P. R. Co.*, 181 Iowa 310, 164 N. W. 747.

⁶⁴ Apparent authority of agents of surety company to sign bond, see *Mills v. Title Guaranty & Surety Co.*, 101 Wash. 162, 172 Pac. 248.

For extensive note on "Liability of a principal for services performed under contract with his agent by persons other than sub-

agents or servants," see L. R. A. 1918 F 8-137.

⁶⁵ *Garland Corporation v. Waterloo Loan & Trust Co.*, 185 Iowa 190, 170 N. W. 373.

⁶⁶ *Lancaster v. Futrell*, — Tex. Civ. App. —, 218 S. W. 805.

⁶⁷ *Illinois Surety Co. v. Donaldson*, 202 Ala. 183, 79 So. 667.

⁶⁸ *E. Clemens Horst Co. v. Peter Breidt City Brewery*, — N. J. L. —, 109 Atl. 727.

⁶⁹ *Southern Surety Co. v. Kinney*, — Ind. App. —, 127 N. E. 575.

⁷⁰ *Emerson v. Fisher*, 246 Fed. 642.

§ 1943. Presumptions and burden of proof—In general.⁷¹ Generally there is no presumption of authority and the burden of proof as to the power of the officer is on the other party to the contract.⁷² A fortiori, the authority of officers of a non-business corporation to bind it will not be presumed and must be specifically proved.⁷³ On the other hand, as a general rule, "where an act has been done or an instrument executed which is within the power of the corporation, and by its appropriate officer or agent, acting ostensibly in its behalf, antecedent authority will be presumed, at least prima facie, so as to make it unnecessary to produce evidence thereof until the presumption is rebutted," especially after the lapse of a great length of time.⁷⁴ Of course, any presumption that certain corporate officers had authority to sign a petition is overcome by their testimony that they had no authority to sign.⁷⁵

§ 1944. — Presumptions from seal. A seal is prima facie evidence that the officers signing did not exceed their authority;⁷⁶

⁷¹ See also § 3093, *infra*.

Effect of affidavit denying assignment of note, on burden of proof, see *Nokomis Nat. Bank v. Hendricks*, 205 Ill. App. 54.

⁷² In suits on promissory notes, the burden is on plaintiff to show that the officer who signed was authorized to sign the name of the corporation. *Ichelson v. S. Schlein & Sons*, 103 N. Y. Misc. 673, 171 N. Y. Supp. 2.

The burden is on plaintiff, in an action for goods sold and delivered a corporation, to show that the person with whom the contract was made was at the time an authorized representative of the defendant corporation. *Shelton Tack Co. v. Reliable Metal Box Mfg. Co.*, — N. Y. Misc. —, 177 N. Y. Supp. 163.

An unsealed deed is not admissible in evidence without showing the authority of the officers execut-

ing it. *Fischer v. Lukens*, — Cal. App. —, 182 Pac. 967.

A corporate lease cannot be introduced in evidence without first proving the authority of the person signing to execute it for the corporation, it is held in *Arkansas. Salmon v. Boyer*, 139 Ark. 236, 213 S. W. 383.

⁷³ *Brown v. Actors' Fund*, 103 N. Y. Misc. 578, 171 N. Y. Supp. 682.

⁷⁴ *Atlanta & C. Air Line R. Co. v. Limestone-Globe Land Co.*, — S. C. —, 96 S. E. 188, applying rule to execution of deed by president.

⁷⁵ *Walton v. Commissioners of Light Improvement Dist. No. 1, City of Benton*, — Ark. —, 222 S. W. 1056.

⁷⁶ *Sovereign Camp v. Burrell*, — Ala. —, 85 So. 762; *Anderson v. Wickliffe*, 178 Cal. 120, 172 Pac. 381; *Macknight v. Davitt*, 37 Cal. App. 720, 174 Pac. 77; *Ross v.*

but the fact that a paper signed by the president and secretary is under the corporate seal is not conclusive evidence of the power of the officers to execute the paper although it raises a presumption of authority.⁷⁷ A sealed contract signed by president and secretary is presumptively signed by the incumbents of such offices.⁷⁸ A deed purporting to have been signed by a corporation by both its president and its secretary, with the corporate seal affixed, is *prima facie* evidence that its execution was by authority of the corporation, although only the signature of the secretary was properly attested.⁷⁹

In California, a copy of a deed reciting that the grantor has "caused its common seal to be affixed by its president, thereunto duly authorized by resolution of its board of directors," is not evidence of such authority, where the copy offered in evidence does not show that the original was under seal.⁸⁰

§ 1945. Question of power as one of law or fact. Authority of officers and agents is generally a question of fact for the jury.⁸¹ Express authority of an agent in charge of the principal office to contract for merchandise, where the evidence is conflicting, is a question for the jury.⁸²

§ 1946. Who may urge want of power. Want of power of a corporate officer to transfer property may be shown by one to whom the property had previously been transferred notwithstanding the corporation does not complain.⁸³

Sutter, — Tex. Civ. App. —, 223 S. W. 273; Lawrence v. Montgomery Gas Co., — W. Va. —, 99 S. E. 496.

Where a mortgage is signed by the proper corporate officers under the corporate seal, it is presumed that they were authorized to make the mortgage. Jump v. Barr, — Cal. App. —, 189 Pac. 334.

Authority of high corporate officers who sign a deed under corporate seal is presumed and the burden is on the corporation to show want of authority. Lawrence v. Montgomery Gas Co., — W. Va. —, 99 S. E. 496.

⁷⁷ Coleman v. Northwestern Ins. Co., 273 Mo. 620, 201 S. W. 544.

⁷⁸ Arnold v. LaBelle Oil Co., — Cal. App. —, 190 Pac. 815.

⁷⁹ Frazier v. Swain, 147 Ga. 654, 95 S. E. 211.

⁸⁰ Fischer v. Lukens, — Cal. App. —, 182 Pac. 967.

⁸¹ Carter v. United States Coal & Coke Co., — W. Va. —, 100 S. E. 405.

⁸² Faber-Musser Co. v. William E. Dee Clay Mfg. Co., 291 Ill. 240, 126 N. E. 186.

⁸³ Burgess Battery Co. v. Solar Light Co., 266 Fed. 368.

XII. DELEGATION OF AUTHORITY BY DIRECTORS OR OTHER OFFICERS OR AGENTS

§ 1952. Delegation of authority by directors or trustees—General rule. The fact that a statute commits the management of corporations to a board of directors does not preclude the appointment of officers by it with certain defined duties which they may exercise.⁸⁴ The “modern method of transacting corporate business requires that agents frequently, in cases where action by the board of directors would be impracticable or unfeasible, represent the corporation in dealings requiring the exercise of a great degree of discretion.”⁸⁵ A contract by several manufacturing corporations creating an executive committee to represent them in negotiations with employees is not invalid as an attempt to delegate discretionary corporate functions.⁸⁶

§ 1953. — Power to delegate entire control. Directors may, it seems, delegate all their powers to an executive committee.⁸⁷

XIII. POWERS OF DIRECTORS

§ 1961. General rules. Directors have “as much control over the business affairs of a corporation as has an individual over his own business, but not more so.”⁸⁸ The contract of directors in the name of the corporation is the contract of the corporation.⁸⁹

§ 1966. Power to elect officers, employ agents or hire employees. Directors may employ counsel and a stenographer to contest an action by minority stockholders, although the majority interests are charged with fraud.⁹⁰

⁸⁴ *Bradley v. Nevada-California-Oregon Ry.*, 42 Nev. 411, 178 Pac. 906.

⁸⁵ *Dyer Bros. Golden West Iron Works v. Central Iron Works*, — Cal. —, 189 Pac. 445, citing 3 *Fletcher Cyc. Corp.*, § 1952.

⁸⁶ *Dyer Bros. Golden West Iron Works v. Central Iron Works*, — Cal. —, 189 Pac. 445.

⁸⁷ *Haldeman v. Haldeman*, — Ky. —, 197 S. W. 376.

⁸⁸ *Merchants' Life Ins. Co. v. Griswold*, — Tex. Civ. App. —, 212 S. W. 807.

⁸⁹ *Fox v. Seattle Contact Copper Co.*, 98 Wash. 557, 168 Pac. 185.

⁹⁰ *Taylor v. Rosehill Cemetery Co.*, 210 Ill. App. 209.

§ 1968. Borrowing money and executing notes or bonds therefor. A board of directors has power to borrow money to pay its debts or to carry on its business and to secure the loan by a deed of trust.⁹¹ It may authorize the execution of a note without ratification by the stockholders.⁹²

Where the acts of directors in personally borrowing money for the corporation were ratified by the stockholders so as to bind the corporation, so far as money borrowed "to carry on the present business" was concerned, the quoted words refer to business conducted by the corporation at the time and not the business which the corporate articles authorized.⁹³

§ 1971. Sales in ordinary course of business. Property of a corporation, or interests therein, can be transferred only by its board of directors or some one duly authorized to act for it.⁹⁴ A director in charge of the buying and selling of the bonds of the corporation may, under some circumstances, have authority to warrant to a buyer the value of the bonds.⁹⁵

§ 1972. Transfer of choses in action. Directors who indorse corporate paper are usually held not to be primary makers or disintituled to presentment and demand by the mere fact of their interest in the corporation.⁹⁶

§ 1985. Acts of bankruptcy—Filing voluntary proceeding in bankruptcy. The board of directors may file a voluntary petition in bankruptcy.⁹⁷ Filing a voluntary petition in bankruptcy is not an "incumbrance" of its property within the Colorado statutes providing that directors of a mining company shall not incumber its mines or plant without consent of the stockholders.⁹⁸

⁹¹ Hartley v. Ault Woodenware Co., 82 W. Va. 780, 97 S. E. 137.

⁹² Western Nat. Bank v. Wittman, 31 Cal. App. 615, 161 Pac. 137.

⁹³ Foley v. Lyman, 183 Iowa 1306, 168 N. W. 153.

⁹⁴ Dickinson Island Land Co. v. Hill, 210 Mich. 53, 177 N. W. 142.

⁹⁵ Burtch v. Child, Hulswit & Co., 207 Mich. 205, 174 N. W. 170.

⁹⁶ Murray v. Third Nat. Bank, 234 Fed. 481.

⁹⁷ Fitts v. Custer Slide Mining & Development Co., 266 Fed. 864; In re S. & S. Manufacturing & Sales Co., 246 Fed. 1005.

Whether directors have power to file a petition of voluntary bankruptcy depends on the law of the state where the company was created. Fitts v. Custer Slide Mining & Development Co., 266 Fed. 864.

⁹⁸ Fitts v. Custer Slide Mining & Development Co., 266 Fed. 864.

§ 1988. Actions. Directors have power to waive a statute of limitations against a just debt,⁹⁹ or to appropriate a reasonable sum to defend an action to put the corporation in the hands of a receiver.¹

§ 1991. Right to inspect corporate books and papers. A director has the right at any time to inspect the corporate books.²

§ 1995. Changes in the corporation or matters not within its regular business—Amendment or alteration of charter. Directors, as distinguished from the stockholders, cannot amend the charter in a fundamental manner.³

§ 1998. — Sale or lease of entire property.⁴

XV. POWERS OF PRESIDENT

§ 2006. General considerations.⁵ Dealing with a man who happens to be president of a bank does not, of course, necessarily make his acts those of the bank, since he may be dealing for himself personally.⁶ A promise by the president of a corporation, where without consideration, is not binding on the company.⁷

§ 2007. Express authority. Where new and additional action was taken by the directors relating to the sale of treasury stock, by providing another method of paying debts, there is an implied rescission of authority given the president by the directors to sell such stock to pay debts.⁸

⁹⁹ *Kelly Asphalt Block Co. v. Brooklyn Alcatraz Asphalt Co.*, 190 N. Y. App. Div. 750, 180 N. Y. Supp. 805.

¹ *Atwater v. Elkhorn Valley Coal Land Co.*, 184 N. Y. App. Div. 253, 171 N. Y. Supp. 552.

² *Leach v. Davy*, 199 Mich. 378, 165 N. W. 927.

³ *Allen v. White*, 103 Neb. 256, 171 N. W. 52.

⁴ See § 1206 et seq., supra.

⁵ "Powers of bank president or

vice president" is the title of a lengthy note in 1 A. L. R. 693-714, annotating *Dent v. People's Bank of Imboden*, 118 Ark. 157, 1 A. L. R. 688, 175 S. W. 1154.

⁶ *Haines v. First Nat. Bank*, 89 Ore. 42, 172 Pac. 505.

⁷ *Stagg v. Kansas Free Fair Ass'n*, 105 Kan. 600, 8 A. L. R. 478, 185 Pac. 893.

⁸ *Copper King Min. Co. v. Hanson*, — Utah —, 176 Pac. 623.

§ 2009. Powers in general merely as incident to office. The president has no implied power to obligate the corporation by any act or contract which in effect overrules or revokes action taken by the board of directors in relation to the same matter.⁹ He may accept an account as an account stated.¹⁰

§ 2010. View that president has no greater power than any other director. In Utah, the rule is reiterated that "the president of a corporation ordinarily has only the powers of a director, or such additional powers as may be directly conferred upon him by the board of directors."¹¹

§ 2012. View that president has power or is presumed to have power to act in ordinary course of business—In general. It has been said that the president "has power *prima facie* to do any act which the directors could authorize or ratify."¹² In North Carolina it is said that "it is true that the president of the corporation is *ex vi termini* its general agent."¹³

§ 2015. — District of Columbia rule.¹⁴

§ 2018. — Kansas rule.¹⁵

§ 2025. — New Jersey rule. When "a contract is made in the name of the corporation by the president in the usual course of business, which the directors have the power to authorize and to make, or to ratify after it is made, the presumption is that the contract is binding on the corporation, unless it is shown that the same was not authorized or ratified."¹⁶

⁹ *Humphrey v. Onaway-Alpena Tel. Co.*, 204 Mich. 97, 170 N. W. 1.

¹⁰ *Thompson Bros. Feed Co. v. Neiman Bros. Co.*, 203 Ill. App. 317.

¹¹ *Copper King Min. Co. v. Hanson*, — Utah —, 176 Pac. 623; *Passow & Sons v. Wetherbee*, 50 Utah 243, 167 Pac. 350.

¹² *Hotel Woodward Co. v. Ford Motor Co.*, 258 Fed. 322.

¹³ *Phillips v. Interstate Land Co.*, 174 N. C. 542, 94 S. E. 12.

¹⁴ That the president may make ordinary contracts, see also *Newbold v. Brennan Const. Co.*, 48 App. Cas. (D. C.) 90.

¹⁵ That president cannot bind corporation, see *Stagg v. Kansas Free Fair Ass'n*, 105 Kan. 600, 8 A. L. R. 478, 185 Pac. 893.

¹⁶ *Summit Silk Co. v. Fidelity Trust Co.*, 88 N. J. Eq. 113, 101 Atl. 573.

§ 2032. Inherent powers as dependent on nature of corporation. The president of a gravel road company, it seems, has the same powers as a president of any other private corporation.¹⁷

§ 2033. Apparent authority and powers as general manager.¹⁸ The authority of the president may be extended by general authority conferred on him to manage the business.¹⁹ The promise of the president actually in charge of tearing down a building, that precaution would be taken to protect an adjoining building, is binding on the company.²⁰

§ 2036. Contracts of employment—General rule.²¹ The president has inherent power, in some jurisdictions, to make contracts of employment.²² Especially can he make such contracts where he is in actual charge of the business.²³ But the president of an insurance company has no authority to employ a business manager for a term of years,²⁴ and the president of a construction company has no power to contract to pay one-

¹⁷ Hurricane Tp. Gravel Road Co. v. Bradley, — Mo. App. —, 204 S. W. 1113.

¹⁸ President as "ostensible agent" of stockholder, see Post v. City & County Bank, — Cal. —, 183 Pac. 802.

¹⁹ Passow & Sons v. Wetherbee, 50 Utah 243, 167 Pac. 350.

²⁰ Huber v. H. R. Douglas, Inc., — Conn. —, 108 Atl. 727.

²¹ For note on "Power of president of a corporation to employ, control or discharge agents or subordinates," see 5 A. L. R. 1485-1495.

²² See Schorr v. John T. Shayne & Co., 208 Ill. App. 328; Grimm v. Mt. Carmel Iron Works, 69 Pa. Super. Ct. 136.

The president has power to hire an accountant at a salary of one thousand dollars a month for a period terminable at will, where the books are in bad shape, not-

withstanding the by-laws make the acts of the president subject to the approval of the board of directors and that the salary agreed on exceeded the salary of the president. Warfield v. Wire Wheel Corporation, 184 N. Y. App. Div. 687, 172 N. Y. Supp. 390.

²³ A president who is given "general control and management" of the corporate business has power to employ an insurance adjuster to adjust a fire loss. P. Curtis Ko Eune Co. v. Manayunk Yarn Mfg. Co., 260 Pa. 340, 5 A. L. R. 1483, 103 Atl. 720.

A president appointed superintendent of a gravel road company has authority, it would seem, to hire a man to work on the road. Hurricane Tp. Gravel Road Co. v. Bradley, — Mo. App. —, 204 S. W. 1113.

²⁴ Pierce v. First Nat. Fire Ins. Co., 46 App. Cas. (D. C.) 239.

half of the profits of a big job for personal services, where it is a contract of an extraordinary character.²⁵

§ 2037. — Employment of brokers or sales and purchasing agents. Authority of a president to purchase stock of another company includes power to contract to pay a commission to effect such a purchase.²⁶ The president of an oil company, supervising drilling on a lease, has no implied authority to agree to pay a broker to sell the lease.²⁷

In California, a president has no implied power to employ a broker to sell corporate land;²⁸ nor to sell shares of stock, nor to determine the price for which they should be sold, nor to employ an agent to find purchasers for stock.²⁹

§ 2038. Negotiable paper—In general. Generally it is held that the president has no inherent power to execute negotiable paper,³⁰ even if he owns nearly all of the stock.³¹ A fortiori, he has no power to draw corporate checks in favor of himself.³² In Illinois, however, authority of a president to sign a note is presumed until the contrary appears,³³ and there is some authority so holding in New York.³⁴ In New York, plaintiff makes out a prima facie case, in an action on a note against

²⁵ *Chard v. Ryan-Parker Const. Co.*, 182 N. Y. App. Div. 455, 169 N. Y. Supp. 622.

²⁶ *Conservation Co. v. Stimpson*, — Md. —, 110 Atl. 495.

²⁷ *Caddy Oil Co. v. Sommer*, 186 Ky. 843, 218 S. W. 288.

²⁸ *Butler v. Solano Land Co.*, — Cal. App. —, 188 Pac. 1019.

²⁹ *Rattray v. Wickersheim Implement Co.*, 36 Cal. App. 253, 171 Pac. 964.

³⁰ *Goodman Mfg. Co. v. Mammoth Vein Coal Co.*, 185 Iowa 253, 168 N. W. 912. See *Massie v. Eldorado Gold Star Min. Co.*, 36 Cal. App. 153, 171 Pac. 814.

The president of a railroad company has no authority to execute a trade acceptance. *Midland & N. W. R. Co. v. Midland Mercan-*

tile Co., — Tex. Civ. App. —, 216 S. W. 627.

³¹ *Goodman Mfg. Co. v. Mammoth Vein Coal Co.*, 185 Iowa 253, 168 N. W. 912.

³² *McCullam v. Mermod, Jaccard & King Jewelry Co.*, — Mo. App. —, 218 S. W. 345, holding also that indorsee of such a check is not a holder in due course within the Negotiable Instruments Law.

³³ *Wells v. Manufacturers & Merchants Life Ass'n*, 213 Ill. App. 549.

³⁴ Notes signed by the president are presumptively authorized. Want of authority must be pleaded and proved as a defense. *Ichelson v. S. Schlein & Sons*, 103 N. Y. Misc. 673, 171 N. Y. Supp. 2.

a trading corporation, signed by the president, but which does not bear the corporate seal, by the mere production of the note without any proof as to the authority of the president.³⁵ There is a presumption, where a corporate note is signed by the president and secretary as such, and it is admitted that the corporation received the consideration, that they had authority to sign.³⁶

§ 2040. — Indorsement of negotiable paper. The president of a corporation has authority to indorse checks payable to the company, but where he deposits such checks to his personal account the depositing bank acts at its peril.³⁷

§ 2042. Purchases. The president of a lumber company has no presumed power to purchase or subscribe for the bonds or stock of another corporation.³⁸ It is held in particular cases that the president has no implied power to sell treasury stock,³⁹ nor to exchange corporate lands,⁴⁰ nor to give an option for the purchase of all the corporate assets,⁴¹ nor to assign a patent owned by the company.⁴²

However, a deed executed by the president and cashier of a bank binds the bank, where all their acts are acquiesced in by the directors.⁴³ So in some states antecedent authority of the president or like officer to execute a deed is presumed so as to make it unnecessary to produce evidence thereof until the presumption is rebutted.⁴⁴

³⁵ Westchester Mortg. Co. v. Thomas B. McIntire, Inc., 174 N. Y. App. Div. 446, 161 N. Y. Supp. 390, holding, however, that this rule does not apply to a nonbusiness corporation.

³⁶ Union Trust Co. v. Ensign-Baker Refining Co., 29 Cal. App. 641, 157 Pac. 613.

³⁷ Wagner Trading Co. v. Battery Park Nat. Bank, 228 N. Y. 37, 9 A. L. R. 340, 126 N. E. 347, aff'g 184 N. Y. App. Div. 885, 170 N. Y. Supp. 1117, and see § 1929, *supra*.

³⁸ Wyoming Construction & De-

velopment Co. v. Buffalo Lumber Co., — Wyo. —, 166 Pac. 391.

³⁹ Copper King Min. Co. v. Hanson, — Utah —, 176 Pac. 623.

⁴⁰ Leo G. McLaughlin Co. v. Phillips, — Cal. —, 189 Pac. 788.

⁴¹ Superior Min. Co. v. White Coal Co., 214 Ill. App. 381.

⁴² Burgess Battery Co. v. Solar Light Co., 266 Fed. 368.

⁴³ Farmers' & Mechanics' Bank v. Western Loan & Building Co., 103 Wash. 349, 174 Pac. 1.

⁴⁴ Atlanta & C. Air Line R. Co. v. Limestone-Globe Land Co., 109 S. C. 444, 96 S. E. 188.

§ 2044. Gifts and dedications. Where no corporate creditor objects, and two persons own all the stock of a corporation, one may, as president, make a deed of gift of the corporate lands to himself and the other stockholder.⁴⁵

§ 2046. Assignments for benefit of creditors. The president has no power to make an assignment for benefit of creditors.⁴⁶

§ 2047. Leases or contracts of hire. The president of a manufacturing corporation has no inherent or apparent power to make a three-year lease.⁴⁷

§ 2048. Mortgage or pledge. A president has no inherent power to mortgage real estate,⁴⁸ although it seems to be held in one case that the president is presumed to have had authority to execute a chattel mortgage where he has already executed it.⁴⁹ The president of a corporation who has full control and management of its affairs, and who borrows money and pledges its property without objection by the board of directors, has implied power to secure a loan by executing a chattel mortgage on the company's property.⁵⁰

§ 2049. Guaranty or promise to pay debt of another. The president of a bank has no authority to obligate it as guarantor, surety or indorser.⁵¹

§ 2050. Modification or rescission of contracts, and waiver. The president has no authority to waive performance of a contract for services.⁵²

⁴⁵ *City of Ft. Worth v. National Park Bank of New York*, 261 Fed. 817.

⁴⁶ *Bell & Co. v. Vogt*, 87 Ore. 102, 168 Pac. 724.

⁴⁷ *Spitzer v. Born*, 111 N. Y. Misc. 595, 182 N. Y. Supp. 327.

⁴⁸ *First Nat. Bank v. Casselton Realty & Investment Co.*, — N. D. —, 175 N. W. 721, citing *Fletcher Cyc. Corp.*, § 2048.

⁴⁹ *Peyton v. Sturgis*, — Tex.

Civ. App. —, 202 S. W. 205, which is not at all clear on this point as to just what is attempted to be decided.

⁵⁰ *P. R. Sinclair Coal Co. v. Missouri-Hydraulic Min. Co.*, — Mo. App. —, 207 S. W. 266.

⁵¹ *Commonwealth Trust Co. v. First-Second Nat. Bank*, 260 Pa. 223, 103 Atl. 598.

⁵² *Wray v. Tilden Saw Co.*, 198 Mich. 461, 164 N. W. 545.

§ 2051. **Compromises and settlements.** The president may, it seems, settle pending litigation, at least in some cases.⁵³ The president and vice president may make a settlement of accounts of one dealing with the corporation.⁵⁴

§ 2052. **Payments.** A tender is properly made to the president and need not be made to the board of directors.⁵⁵ Power conferred on the president of a corporation to "pay the bills" of the company, with certain funds, authorizes him to pay a debt barred by limitations and held by a corporation in which the president was the sole stockholder, where all those interested know all the facts and no one objects.⁵⁶ A president has no authority to accept, as payment for a corporate debt, a note for his individual debt.⁵⁷ The president of a bank cannot withdraw money of a depositor without his authority, and if he does so the bank is liable for his wrongful act.⁵⁸

§ 2053. **Releases.** The president has no power to release corporate debtors.⁵⁹ The president and cashier of a bank cannot release signers of a note held by the bank.⁶⁰

§ 2054. **Legal proceedings—In general.**⁶¹ A president who performs the duties of treasurer can sign proof of claim in bankruptcy although the rules require the treasurer to sign.⁶² The president of a bank has incidental authority to submit claims of the bank against a decedent's estate to the appropriate

⁵³ *Dickinson v. Citizens' Ice & Fuel Co.*, 139 Minn. 201, 165 N. W. 1056.

⁵⁴ *American Clay & Cement Corporation v. Rochester Folding Box Co.*, 171 N. Y. Supp. 720.

⁵⁵ *Union Building Loan Fund & Savings Ass'n v. Block*, — Ind. App. —, 127 N. E. 775.

⁵⁶ *Kelly Asphalt Block Co. v. Brooklyn Alcatraz Asphalt Co.*, 190 N. Y. App. Div. 750, 180 N. Y. Supp. 805.

⁵⁷ *Wood v. Hendon*, 16 Ala. App. 327, 77 So. 921.

⁵⁸ *DeWar v. First Nat. Bank of Roseburg*, 88 Ore. 541, 171 Pac. 1106.

⁵⁹ *W. G. Zachow Co. v. Grignon*, — Wis. —, 179 N. W. 593.

⁶⁰ *Bank of Dexter v. Simmons*, — Mo. App. —, 204 S. W. 837.

⁶¹ Whether president of ordinary commercial corporation has authority to answer interrogatories in garnishment was deemed a doubtful question in *Hibernia Bank & Trust Co. v. Dresser*, 145 La. 133, 81 So. 875.

⁶² *In re Eisenberg*, 251 Fed. 427.

court in a foreign jurisdiction.⁶³ Acceptance of service of summons or of notices in general is within the power of a president.⁶⁴ He has power to employ counsel to defend the corporation, at least where given general charge of the business affairs of the corporation.⁶⁵

§ 2055. — Power to confess judgment. The president has no power, by virtue of his office alone, to sign a warrant of attorney to confess judgment;⁶⁶ but it is held that the burden of proving that he was not expressly or impliedly given authority to sign a warrant of attorney to confess judgment is on the party making such claim.⁶⁷

XVI. POWERS OF VICE PRESIDENT

§ 2063. In general. A vice president, if held out as a general manager, may execute contracts, etc.⁶⁸ The vice president of a railroad company, where also its general manager, has power to contract for fencing the track, at least in case of an emergency.⁶⁹ The vice president of a bank, although intrusted with its general management, cannot bind the bank in a matter so out of the usual course of business as to put on notice the other party to the deal that he is using the name of the bank in his own business.⁷⁰

§ 2070. Presumptions. In Texas, a vice president who has signed a chattel mortgage will be presumed to have had authority so to do, although he has no inherent authority to do such an act.⁷¹

⁶³ *Old Dominion Trust Co. v. First Nat. Bank*, 260 Fed. 22.

⁶⁴ See *Hart Land & Improvement Co. v. Odd Fellows Hall Ass'n*, 142 La. 487, 77 So. 125.

⁶⁵ *Blue Goose Min. Co. v. Northern Light Min. Co.*, 245 Fed. 727.

⁶⁶ *State Bank of East Moline v. Moline Pressed Steel Co.*, 283 Ill. 581, 119 N. E. 604.

⁶⁷ *State Bank of East Moline v. Moline Pressed Steel Co.*, 283 Ill. 581, 119 N. E. 604.

⁶⁸ *Alabama City, G. & A. R. Co. v. Kyle*, 202 Ala. 552, 81 So. 54.

⁶⁹ *Bradley v. Nevada-California-Oregon Ry.*, 42 Nev. 411, 178 Pac. 906.

⁷⁰ *First Nat. Bank v. Drovers' & Mechanics' Nat. Bank*, 244 Fed. 135.

⁷¹ *Peyton v. Sturgis*, — Tex. Civ. App. —, 202 S. W. 205.

XVII. POWERS OF SECRETARY

§ 2071. Powers and duties in general—Nature of office. The secretary has authority to write a letter for the corporation as provided for by the board of directors.⁷² A secretary and book-keeper of a company has no power to sign papers or make entries in the nature of a trust in land.⁷³ A person appointed by the directors to act in the absence of the secretary may execute a corporate instrument in the capacity of secretary.⁷⁴

§ 2073. — Express or apparent authority.⁷⁵ A secretary has no implied authority to contract for the corporation.⁷⁶

§ 2074. Contracts of employment. The secretary has no authority to employ salesmen.⁷⁷

§ 2076. Negotiable paper.⁷⁸ It will be presumed that one holding the office of secretary and treasurer has power to sign a note for the corporation.⁷⁹ A secretary has no power to indorse checks payable to the corporation,⁸⁰ nor to deposit a corporate check in his own account.⁸¹ Authority conferred on the secretary to sign contracts, receipts, acceptances, etc., does not confer power to indorse checks belonging to the corporation.⁸²

⁷² Great Western Mfg. Co. v. Porter, 103 Kan. 84, 172 Pac. 1018.

⁷³ Austin v. Young, 90 N. J. Eq. 47, 106 Atl. 395.

⁷⁴ Arnold v. LaBelle Oil Co., — Cal. App. —, 190 Pac. 815.

⁷⁵ Apparent authority of secretary to make contract, see Shpunt v. Machinery Merchants, 112 N. Y. Misc. 457, 183 N. Y. Supp. 90.

Apparent authority of secretary to draw checks payable to himself, see Napoleon Hill Cotton Co. v. H. Oelter Grocery Co., — Mo. App. —, 222 S. W. 876.

⁷⁶ Hopkins v. Paradise Heights Fruit Growers' Ass'n, — Mont. —, 193 Pac. 389.

⁷⁷ McAllister v. Pittsburgh Water Heater Co., 65 Pa. Super. Ct. 522.

⁷⁸ Notice where corporate paper deposited in individual account of secretary, see § 1929, supra.

⁷⁹ Swift & Co. v. Dawson Paper Shell Pecan Co., — Ga. App. —, 101 S. E. 754.

⁸⁰ McCabe Hanger Mfg. Co. v. Chelsea Exchange Bank, 167 N. Y. Supp. 580.

⁸¹ Buena Vista Oil Co. v. Park Bank, 39 Cal. App. 710, 180 Pac. 12.

⁸² McCabe Hanger Mfg. Co. v. Chelsea Exchange Bank, 167 N. Y. Supp. 580.

§ 2078. **Assignments.** One discharging the duties of secretary and treasurer has no implied power to accept a partial assignment of a debt due by it.⁸³

§ 2079. **Pledge or mortgage.** One holding the office of secretary and treasurer is not presumed to have power to execute a chattel mortgage.⁸⁴ So the secretary cannot mortgage real estate.⁸⁵

§ 2081. **Releases.** A corresponding secretary of a religious society is not the "president or presiding member or trustee" so as to be authorized to release a mortgage.⁸⁶

§ 2082. **Guaranty or indemnity.** A secretary has no authority to guarantee notes.⁸⁷

§ 2086. **Certificates.** An assistant secretary of a corporation may sign the affidavit for a mechanic's lien.⁸⁸

XVIII. POWERS OF TREASURER

§ 2087. **In general.**⁸⁹ The selling agent and treasurer of a corporation are not presumed to be authorized to adjust with an insurance company the amount of a loss by fire.⁹⁰ A comptroller of a traction company who is the supervisor of both the auditing and treasury departments is not, as a matter of law, without authority to make a special promise to pay persons furnishing lumber to a contractor doing work for the corporation.⁹¹

⁸³ Sheatz v. Markley, 249 Fed. 315.

⁸⁴ Peyton v. Sturgis, — Tex. Civ. App. —, 202 S. W. 205.

⁸⁵ First Nat. Bank v. Casselton Realty & Investment Co., — N. D. —, 175 N. W. 721, citing Fletcher Cyc. Corp. § 2091.

⁸⁶ Alling v. Vander Stucken, — Tex. Civ. App. —, 194 S. W. 443.

⁸⁷ Advance Rumely Thresher Co. v. Evans Metcalf Implement Co., 103 Kan. 532, 175 Pac. 392.

⁸⁸ Rogers-Templeton Lumber Co. v. Welch, — Mont. —, 184 Pac. 838.

⁸⁹ Powers of officer who is both secretary and treasurer, see §§ 2076, 2078, 2079, *supra*.

⁹⁰ Victoria Park Co. v. Continental Ins. Co., 39 Cal. App. 347, 178 Pac. 724.

⁹¹ Cincinnati Traction Co. v. Cole, 258 Fed. 169, 179.

§ 2089. Negotiable paper. A treasurer is *prima facie* the proper officer to sign a note for the corporation.⁹² Power conferred on the treasurer to indorse notes and checks does not, it seems, authorize him to execute notes.⁹³

XIX. POWERS OF GENERAL MANAGER, SUPERINTENDENTS, BRANCH MANAGERS AND THE LIKE

§ 2096. Definitions and general considerations.⁹⁴ A “managing officer” is not necessarily one of the head executive officers but is any one to whom the corporation has committed the general management or general superintendence of the whole or a particular part of a business.⁹⁵

§ 2097. Kinds of and classification. A general manager of a business corporation is one who has the general direction and control of the affairs of the corporation as distinguished from one having the management of some particular branch of the business.⁹⁶ A person called a “superintendent” is not necessarily a general manager.⁹⁷

§ 2098. Powers in general—Statement of rule. The powers of a general manager, although large and extensive, are not unlimited.⁹⁸ However, he has general authority to perform

⁹² *Swift & Co. v. Dawson Paper Shell Pecan Co.*, — Ga. App. —, 101 S. E. 754.

⁹³ *Martin v. Interstate Lumber Co.*, 260 Pa. 218, 103 Atl. 613.

⁹⁴ Definition of manager, see *Pilgrim Health & Life Ins. Co. v. McIntosh*, — Ga. App. —, 100 S. E. 40.

⁹⁵ *The Erie Lighter* 108, 250 Fed. 490.

⁹⁶ *Braman, Dow & Co. v. Kennebec Gas & Fuel Co.*, 117 Me. 291, 104 Atl. 3.

⁹⁷ *New York City v. Staten Island Midland Ry. Co.*, — N. Y. Misc. —, 180 N. Y. Supp. 1.

⁹⁸ *Dixie Industrial Co. v. Atlas Lumber Co.*, 202 Ala. 556, 81 So.

64; *Carroll-Cross Coal Co. v. Abrams Creek Coal & Coke Co.*, 83 W. Va. 205, 98 S. E. 148, citing *Fletcher Cyc. Corp.* §§ 2096, 2098.

The powers of managing officers, whoever they may be, are coextensive with those of the board of directors, except in relation to matters over which the stockholders alone have control. *Depot Realty Syndicate v. Enterprise Brewing Co.*, 87 Ore. 560, L. R. A. 1918 C 1001, 170 Pac. 294. This statement, however, is too broad.

A corporation which trusts to an officer “the general management of the business should be held bound by his acts, even though he went beyond his delegated powers.

all reasonable things in conducting the usual and customary business of his principal.⁹⁹ A general manager "may do in the transaction of its ordinary affairs what the corporation itself could do within the scope of its powers."¹

The general manager of a water company has authority to order disconnection of the supply pipe of a customer, to force payment of an account.²

§ 2101. — Manager of branch or department. A branch manager of a mining stock brokerage company has implied authority to retain for payment of assessments and resale certificates of mining stock purchased through him.³ Where acts are out of the usual course of business, persons dealing with a branch manager must inquire as to his authority or deal with him at their peril.⁴

§ 2102. Contracts in general—Statement of rule. A general manager has power to make ordinary contracts pertaining to the business,⁵ or at least is presumed to have power to enter into contracts in the usual course of business.⁶ Contracts made

if by reason of a want of the exercising of due care it failed in its duty to know in what manner Beck was handling its correspondence." *Berthold & Jennings Lumber Co. v. Texas Hardwood Lumber Co.*, — Mo. App. —, 209 S. W. 591.

⁹⁹ *Hinton v. D'Yarmett*, — Tex. Civ. App. —, 212 S. W. 518.

¹ *Raftis v. McCloud River Lumber Co.*, 35 Cal. App. 397, 170 Pac. 176.

² *Eutaw Ice Water & Power Co. v. McGee*, 16 Ala. App. 652, 81 So. 144.

³ *Sullivan v. Evans-Morris-Whitney Co.*, — Utah —, 180 Pac. 435, where manager had converted the stock.

⁴ *J. I. Case Threshing Mach. Co. v. Dallas Chamber of Commerce*, — Tex. Civ. App. —, 206 S. W. 206.

⁵ *Raftis v. McCloud River Lum-*

ber Co., 35 Cal. App. 397, 170 Pac. 176; *Morris v. Basnight*, 179 N. C. 298, 102 S. E. 389; *Carroll-Cross Coal Co. v. Abrams Creek Coal & Coke Co.*, 83 W. Va. 205, 98 S. E. 148, citing *Fletcher Cyc. Corp.* § 2102.

A general manager has power to make contracts for the corporation which the latter could make. *Cuero Packing Co. v. Alamo Mfg. Co.*, — Tex. Civ. App. —, 194 S. W. 492. This statement is too broad.

The general manager of a coal mining company has power to make such contracts as are reasonably necessary in conducting the business of mining and selling coal. *Producers' Coal Co. v. Mifflin Coal Min. Co.*, 82 W. Va. 311, 95 S. E. 948.

⁶ *Michie Grocery Co. v. Martin*, — Cal. App. —, 188 Pac. 615.

by a general manager are not within his implied authority where not usual ones in the ordinary course of business.⁷ A resolution of directors providing that the powers of the general manager should be exercised under the direction of the president does not mean that the president must sanction every detail of every transaction as a condition precedent to the authority of the manager to contract.⁸

An agent of a stock yards company, in general charge of its local business, has apparent authority to contract for keeping and feeding at local yards the cattle of another without expense to him.⁹ A general manager of a coal mine has power to agree with a fruit company owning the surface of the land as to paying for trees destroyed in the process of mining,¹⁰ but he has no power to give, sell, trade or release any part of the leasehold estate.¹¹ A vice president of a bank, intrusted with the general transaction of the business of the bank, has authority to borrow money, make or indorse notes therefor, and

⁷ *Rasnick v. W. M. Ritter Lumber Co.*, 187 Ky. 523, 219 S. W. 801; *Miley v. Heaney*, 168 Wis. 58, 169 N. W. 64.

Whether a particular contract made by a general manager is within his implied power depends on whether its execution is reasonably necessary to, and customary and usual in, the performance of the duties to be discharged by managers. *Napier v. Mozena Coal Co.*, — W. Va. —, 103 S. E. 125.

Even a general manager of a bank cannot bind it in regard to transactions outside the usual course of business. *Drovers' & Mechanics' Nat. Bank v. First Nat. Bank*, 260 Fed. 9.

A superintendent of a mine, with power to make work contracts, has no implied power to agree to furnish money to one employed to haul coal for the company, to enable him to redeem from execution his teams used to haul coal, where it does not appear that such agree-

ments are usual or customary under similar circumstances. *Napier v. Mozena Coal Co.*, — W. Va. —, 103 S. E. 125.

If transactions of the vice president of a bank, who is in reality in charge of the bank, with another bank, are so out of the usual course of business as to put the latter bank on notice that he is acting beyond his authority, or using the bank's name in his own interest, he cannot bind his bank. *Drovers' & Mechanics' Nat. Bank v. First Nat. Bank*, 260 Fed. 9.

⁸ *Simpson v. Malter*, — Cal. App. —, 185 Pac. 675.

⁹ *Sioux Falls Stock Yards Co. v. Ash*, — S. D. —, 177 N. W. 761.

¹⁰ *Fairview Fruit Co. v. H. P. Brydon & Bro.*, — W. Va. —, 102 S. E. 231.

¹¹ *Carroll-Cross Coal Co. v. Abrams Creek Coal & Coke Co.*, 83 W. Va. 205, 98 S. E. 148, citing *Fletcher Cyc. Corp.* §§ 2096, 2098.

assign its bills receivable as security in the usual course of business.¹²

§ 2104. Contracts of employment—In general. A general manager with power to sell threshing machines has power to employ assistants in making the sale and to arrange for a reasonable commission for them.¹³ A general manager who is the controlling stockholder has power to employ one to secure funds for the corporation and to promise to compensate him therefor.¹⁴ A branch manager of a moving picture exchange has power to orally contract for services outside of those covered by a written contract, calling for a different class of work to be paid for on a different basis, where not interfering with the services to be rendered under the written contract.¹⁵

§ 2105. — Employment of superintendent or other general agent. Employment of an assistant manager by the president and manager is presumptively authorized without showing authority from the board of directors.¹⁶

§ 2106. — Employment of brokers or agents to buy or sell. The general manager of an explosives company has power to employ brokers to sell explosives.¹⁷ But a general manager has no implied power to agree to pay a real estate broker for services in selling the entire plant.¹⁸ The secretary of a family corporation, who runs the business and is practically the corporation itself, has power to employ one to procure a loan upon

¹² *Drovers' & Mechanics' Nat. Bank v. First Nat. Bank*, 260 Fed. 9.

¹³ *Kopan v. Minneapolis Threshing Mach. Co.*, 39 N. D. 27, 166 N. W. 826.

¹⁴ *Wolf v. Ideal Sheet Metal Works*, 209 Ill. App. 252.

¹⁵ *Malone v. Pathe Exchange*, 141 Minn. 339, 170 N. W. 215.

¹⁶ *Grummet v. Fresno Glazed Cement Pipe Co.*, — Cal. —, 185 Pac. 388, where by-laws gave president direction of the affairs of the cor-

poration "subject to the advice of the directors."

¹⁷ *Bassick v. Aetna Explosives Co.*, 246 Fed. 974.

¹⁸ *Brooke v. Cartersville Chero-Cola Bottling Co.*, 23 Ga. App. 671, 99 S. E. 150.

A superintendent of a manufacturing plant has no authority to sell the property and hence no authority to employ a broker to sell it. *Cusick v. Worthington Pump & Machinery Corporation*, 169 Wis. 509, 173 N. W. 212.

certain property and agree to pay a certain commission therefor, where no meeting of the directors had been held for some five years.¹⁹

A general manager has no power to sell shares of stock, or to determine the price for which they should be sold, or to employ an agent to find purchasers for stock.²⁰

§ 2108. — For what length of time contracts of employment may be made. Where a director takes over the general management of the business, he has authority to hire for a year one to manage the bowling alleys of the corporation.²¹

§ 2110. Borrowing money. Ordinarily the manager of a branch office has no power to borrow money.²²

§ 2111. Negotiable paper—In general. There are decisions holding that a general manager may execute notes.²³ Whether a general manager has power to execute notes depends on the circumstances of the particular case, it is held in Missouri.²⁴ A general manager has no power to sign notes for stock in another corporation.²⁵

§ 2113. — Indorsement for transfer. A general manager has authority to indorse a note for transfer, but only in furtherance of the corporate business.²⁶ Where a general manager

¹⁹ Koenig v. George Logemann & Sons Co., 170 Wis. 619, 176 N. W. 58.

²⁰ Rattray v. Wickersheim Implement Co., 36 Cal. App. 253, 171 Pac. 964.

²¹ Hartford v. Massachusetts Bowling Alleys, 229 Mass. 30, 118 N. E. 188.

²² Guaranty Bank & Trust Co. v. Beaumont Cadillac Co., — Tex. Civ. App. —, 218 S. W. 638.

²³ MacKay v. Jamestown Gas Co., — N. D. —, 171 N. W. 92; Mitchell Street State Bank v. Froedtert, 169 Wis. 120, 170 N. W. 822.

Where president is general manager, and he transacts all the corporate business, he has power to execute notes. Passow & Sons v. Wetherbee, 50 Utah 243, 167 Pac. 350.

²⁴ Magnolia Compress & Warehouse Co. v. St. Louis Cash Register Co., — Mo. App. —, 210 S. W. 125.

²⁵ United States Printing & Lithographing Co. v. Stovall-Jones Co., 23 Ga. App. 472, 98 S. E. 407.

²⁶ Bank of Benson v. Gordon, 103 Neb. 508, 172 N. W. 367.

has been sent to a distant state in regard to a claim and while there he receives a treasury warrant, he has implied power to indorse and cash it to pay his expenses, especially where he went on the trip unprovided with corporate funds.²⁷

§ 2114. Purchases.²⁸ A general manager has power to buy machinery and execute notes therefor in a proper case.²⁹ The manager of an amusement company is deemed to have power to buy theater furniture, curtains, equipment, etc., where it had been the custom for a long time for him to buy supplies and the corporation had always paid the bills without protest.³⁰ The general manager of a gas company has power to order pipe and fix the terms of payment.³¹

§ 2116. Sales—General rules. A general manager who makes sales has authority to bind the corporation by agreements relating to such sales.³² He has no power to sell all the corporate assets.³³ The "general manager of a corporation has no such plenary power to sell out its entire property and assets as would avoid the necessity of the purchasers inquiring who was really interested in the company, and such inquiries should not have been made solely of the general manager and his colleague."³⁴

§ 2117. — Personal property. A general manager of a seed company has power to warrant seed sold although the custom of the trade was not to warrant seed.³⁵ The fact that a company engaged in the grain, feed and mule business orders a car

²⁷ *Staples v. Port Graham Coal Co.*, 46 App. Cas. (D. C.) 542.

²⁸ Power of general manager of brewing company to buy saloon furnishings, see *Sternberger v. Anheuser-Busch Brewing Co.*, 203 Ill. App. 86.

²⁹ *Dixie Industrial Co. v. Atlas Lumber Co.*, 202 Ala. 556, 81 So. 64.

³⁰ *Southern Amusement Co. v. Ferrell-Bledsoe Furniture Co.*, 125 Va. 429, 99 S. E. 716.

³¹ *Braman, Dow & Co. v. Ken-*

nebec Gas & Fuel Co., 117 Me. 291, 104 Atl. 3.

³² *International Harvester Co. v. Hauelsen*, — Ind. App. —, 118 N. E. 320.

³³ *Empire Coal Min. Co. v. Empire Coal Co.*, 183 Ky. 699, 210 S. W. 474.

³⁴ *Curnen v. Ryan*, 187 N. Y. App. Div. 6, 175 N. Y. Supp. 50.

³⁵ *Moorhead v. Minneapolis Seed Co.*, 139 Minn. 11, L. R. A. 1918 C 391, Ann. Cas. 1918 E 481, 165 N. W. 484.

of soft drinks, puts the proposed seller on inquiry as to the power of the general manager to act in a matter so foreign to the business of his corporation.³⁶ A vice president of a cotton seed oil company held out as manager of its mill has apparent authority to contract to sell 500 bales of linters which is not much in excess of the previous yearly output of the mill, where the contract is not an extraordinary one.³⁷ One in entire charge of the only office a domestic corporation has in the state, the statute requiring a principal office in the state, is presumed to have power to contract for the sale of merchandise within the scope of the ordinary business of the corporation.³⁸

§ 2118. — Real property. A gift, sale or release of a portion of the mining territory to another corporation is not within the implied powers of the general manager of a mining company.³⁹

§ 2120. Gifts and dedications. The manager cannot give away the corporate property,⁴⁰ but a general manager who owns practically all the stock of an improvement company may dedicate lands.⁴¹

§ 2121. Mortgage, pledge or lien. The Alabama statute authorizing directors to execute chattel mortgages does not prohibit execution of such mortgages by one to whom the directors committed the entire management of the corporation.⁴²

§ 2122. Leases and contracts of hire. The general manager of a mercantile business has implied power to execute and renew leases as to the property necessary for carrying on the

³⁶ *St. Louis Beverage Co. v. Planters' Grain Elevator, Mule & Feed Co.*, 198 Mo. App. 284, 200 S. W. 780.

³⁷ *E. I. Du Pont De Nemours & Co. v. Capital City Oil Co.*, 146 La. 720, 84 So. 31.

³⁸ *Faber-Musser Co. v. William E. Dee Clay Mfg. Co.*, 291 Ill. 240, 126 N. E. 186, rev'g 212 Ill. App. 674.

³⁹ *Carroll-Cross Coal Co. v. Abrams Creek Coal & Coke Co.*, 83 W. Va. 205, 98 S. E. 148.

⁴⁰ *Deutsche P. Kirche v. Trustees*, 89 N. J. Eq. 242, 104 Atl. 642.

⁴¹ *Duke Land & Improvement Co. v. Murphy*, 179 N. C. 133, 101 S. E. 497.

⁴² *In re Grocers' Baking Co.*, 266 Fed. 900.

business, such as storehouse, lands, etc.⁴³ A general manager is presumed to have power to reduce the rent of a subtenant in the building where the corporation conducted its business, in order that the corporation might not lose such sublessee and the entire rent.⁴⁴ A general agent with authority to rent lands has apparent power to fix the terms of the rental contracts.⁴⁵ The general manager of a coal company has no implied authority to dispose of or incumber to another company any part of its leasehold estate.⁴⁶

§ 2123. Insurance. A general manager does not necessarily have authority to change the beneficiary in an insurance policy payable to the corporation.⁴⁷

§ 2126. Guaranty or indemnity. A general manager may make a guaranty in the usual course of business,⁴⁸ where within the power of the corporation.⁴⁹ For instance, a general manager has power to guarantee notes of customers given in payment of goods to a third person, on which the corporation gets a commission for the sale, where the obligation was one within the usual course of the corporate business.⁵⁰ So the managing officers of a brewing company (in this case the president and secretary) have power to either authorize or ratify the guaranty of rent under a lease by a third person to a saloon keeper, where the act is not ultra vires.⁵¹ It has even been held that

⁴³ Georgia Casualty Co. v. Massey, 201 Ala. 601, 79 So. 33.

⁴⁴ Sherman, Clay & Co. v. Bufum & Pendleton, 91 Ore. 352, 179 Pac. 241.

⁴⁵ Three States Lumber Co. v. Moore, 132 Ark. 371, 201 S. W. 508.

⁴⁶ Standard Island Creek Coal Co. v. Shamrock Coal Co., — W. Va. —, 104 S. E. 106.

⁴⁷ Coleman v. Northwestern Mut. Life Ins. Co., 273 Mo. 620, 201 S. W. 544.

⁴⁸ C. F. Harms Co. v. Leonhard Michel Brewing Co., 228 N. Y. 263, 126 N. E. 705, rev'g 183 N. Y.

App. Div. 886, 169 N. Y. Supp. 1088. See Weiss v. Fred Bender Store Fixture Co., 207 Ill. App. 72.

That a general manager who is also secretary and treasurer and owns nearly half the corporate stock may guarantee payment of rent by a third person to promote business, see Weiss v. Fred Bender Store Fixture Co., 207 Ill. App. 72.

⁴⁹ Woods Lumber Co. v. Moore, — Cal. —, 191 Pac. 905.

⁵⁰ Advance Rumely Thresher Co. v. Evans Metcalf Implement Co., 103 Kan. 532, 175 Pac. 392.

⁵¹ Depot Realty Syndicate v.

a general manager has implied authority to guarantee payment by an employee for furniture he proposed to buy, in order to retain him as an employee.⁵²

On the other hand, a bank manager has no authority to guarantee payment of a debt by a third person.⁵³ So a branch house manager of a threshing machine company is not impliedly authorized to agree to save a chamber of commerce harmless from loss in promoting a corn show where there is nothing to show the character of the company's business nor the actual authority of such manager.⁵⁴

§ 2129. Releases or modification of contracts. A general manager who makes a sale has power to modify the terms of the contract.⁵⁵ A general manager of an oil-drilling company has authority to modify a drilling contract so as to permit the owner of the land to do the drilling with the equipment of the company.⁵⁶ A mere sales manager has no authority to alter the terms of a written contract made by the corporation.⁵⁷

§ 2131. Compromise and settlement. A superintendent of a sawmill is not authorized to compromise lawsuits filed against employees of the corporation as individuals.⁵⁸

XX. POWERS OF CASHIERS

§ 2138. Cashiers of banks—In general. Cashier of a bank is generally its chief executive officer and its general agent in the transaction of its legitimate business.⁵⁹ A bank cashier

Enterprise Brewing Co., 87 Ore. 560, L. R. A. 1918 C 1001, 170 Pac. 294, 171 Pac. 223.

⁵² M. Burg & Sons v. Twin City Four Wheel Drive Co., 140 Minn. 101, 167 N. W. 300.

⁵³ Merchants Bank of Canada v. Stevens, 49 Dom. L. Rep. (Can.) 528.

⁵⁴ J. I. Case Threshing Mach. Co. v. Dallas Chamber of Commerce, — Tex. Civ. App. —, 206 S. W. 206.

⁵⁵ Ware v. Fairbanks-Morse Co., — Tex. Civ. App. —, 217 S. W. 211.

⁵⁶ Hinton v. D'Yarmett, — Tex. Civ. App. —, 212 S. W. 518.

⁵⁷ Interstate Chemical Co. v. James Leo Co., — N. J. L. —, 110 Atl. 903.

⁵⁸ Rasnick v. W. M. Ritter Lumber Co., 187 Ky. 523, 219 S. W. 801.

⁵⁹ Chapman v. First Nat. Bank, — Wyo. —, 181 Pac. 360. See also Shrader v. McDaniel, 106 Kan. 755, 189 Pac. 954.

It is "not within the apparent scope of the cashier's authority to speak for the board of directors." Reuter v. Nixon State Bank, —

given the entire management of the bank for a considerable time has authority to do anything which the board of directors might have authorized him to do in the first instance, so far as innocent third persons are concerned, although the bank is defrauded by the acts.⁶⁰ He has the apparent power to bind the bank in its usual financial business,⁶¹ but he cannot bind the bank by making a contract with an architect nor for the building of a two-story brick building,⁶² and he has no power to make loans for depositors in the name of the bank.⁶³

The general rule of agency that no person can act as an agent in a transaction in which he has a personal or pecuniary interest applies to the cashier of a bank.⁶⁴

The powers of cashiers of banks are sometimes expressly limited by statutes.⁶⁵

§ 2139. — Acts done outside of bank or of banking hours. The acts of a cashier and manager of a bank, when acting for the bank, are binding on the bank whether such acts take place within the bank building or elsewhere.⁶⁶

§ 2142. — Certification of checks. A cashier has inherent power to certify checks.⁶⁷

§ 2143. — Executing, accepting, etc., negotiable instruments. Whether a cashier of a bank has authority to issue a draft for the debt of a corporation in which he is a stockholder and managing officer, and upon which debt he is a surety, is the subject of conflict in the decisions.⁶⁸

Tex. Civ. App. —, 206 S. W. 715.

⁶⁰ First State Bank v. Lang, — Mont. —, 174 Pac. 597.

⁶¹ Reuter v. Nixon State Bank, — Tex. Civ. App. —, 206 S. W. 715.

⁶² Reuter v. Nixon State Bank, — Tex. Civ. App. —, 206 S. W. 715.

⁶³ Holmes v. Uvalde Nat. Bank, — Tex. Civ. App. —, 222 S. W. 640.

⁶⁴ Choctaw Bank v. Gewin, 16 Ala. App. 349, 78 So. 96.

⁶⁵ See Bank of Kirksville v. Sloop, 198 Mo. App. 225, 200 S. W. 72, transfer of notes, etc., received for money loaned.

⁶⁶ Ravinia State Bank v. Kirkpatrick, — S. D. —, 173 N. W. 863.

⁶⁷ Smith v. Hubbard, 205 Mich. 44, 171 N. W. 546.

⁶⁸ Citizens' Trust Co. v. Abston, Wynne & Co., 242 Fed. 392.

§ 2146. — **Purchases and sales, including transfers of commercial paper.** The cashier of a bank has prima facie authority to transfer notes belonging to the bank,⁶⁹ in the usual course of business.⁷⁰ He is not prohibited by Missouri statutes from selling notes held by the bank in the ordinary course of business.⁷¹

§ 2148. — **Purchase and sales of shares of stock or acceptance thereof in payment.** The cashier of a national bank may be clothed by the board of directors with power to sell corporate shares acquired by the bank as a result of a loan made upon the shares as security.⁷²

§ 2149. — **Pledge or mortgage.** Cashier of a bank has power to receive bonds as collateral on behalf of the bank,⁷³ or to pledge collateral for a debt of the bank.⁷⁴

§ 2151. — **Contracts of employment.** Cashier of a bank has no apparent authority to make a contract with an architect nor for the building of a two-story brick building.⁷⁵

§ 2154. — **Releases.** A cashier of a bank cannot release a debt due the bank.⁷⁶

§ 2155. — **Compromises.** A cashier of a bank has no authority to sign a composition agreement with a debtor.⁷⁷

⁶⁹ Choctaw Bank v. Gewin, 16 Ala. App. 349, 78 So. 96.

⁷⁰ Choctaw Bank v. Gewin, 16 Ala. App. 349, 78 So. 96.

⁷¹ Taylor v. Fuqua, — Mo. App. —, 219 S. W. 971.

⁷² Union Nat. Bank v. McBoyle, 243 U. S. 26, 61 L. Ed. 570, dismissing writ of error to review 168 Cal. 263, 142 Pac. 837.

⁷³ Mitchell Street State Bank v. Schaefer, 169 Wis. 543, 173 N. W. 330.

⁷⁴ Houston Nat. Exchange Bank v. Gregg County, — Tex. Civ. App. —, 202 S. W. 805.

⁷⁵ Reuter v. Nixon State Bank, — Tex. Civ. App. —, 206 S. W. 715.

⁷⁶ First State Bank v. Lang, — Mont. —, 174 Pac. 597.

A cashier, although acting as general manager of a bank, has no power to release security put up by the president, since the latter must show that his dealings with the bank have been fair and honest. First State Bank v. Lang, — Mont. —, 174 Pac. 597.

⁷⁷ Hodiament Bank v. Franklin, — Mo. App. —, 215 S. W. 503.

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§ 2156. — Accepting payments. Cashier of a bank has authority to collect notes due the bank, and a payment to him is not at the risk of the payor even though he does not produce the note.⁷⁸

§ 2157. — Collections and legal proceedings to enforce. A bank cashier has authority to receive commercial paper for collection.⁷⁹

XXI. ADMISSIONS, DECLARATIONS AND REPRESENTATIONS OF OFFICERS AND AGENTS

§ 2161. General rules—Elements making declarations or admissions binding. Admissions of officers are binding on the corporation only where they are acting for the corporation and within the scope of their authority.⁸⁰ The rule that the statements of an officer or agent are not binding on the corporation where he is known to have a personal interest in the transaction apart from his interest or duty as an officer or agent, applies only when the statement is made in his own interest and against the interest of the corporation, to the knowledge of the other party.⁸¹

§ 2162. — Statements as to past events. The president of a bank has no power to bind the bank by statements as to past transactions.⁸² But it has been held that an agent of a corporation, if acting within the scope of his authority, may make an admission in behalf of the corporation as to a past transaction just as a natural person or his authorized agent may do so.⁸³

§ 2164. — Application of rules. Statements of the manager, president and secretary as to ownership of property by the corporation are binding on the company.⁸⁴ Fraudulent repre-

⁷⁸ National Bank v. Whitney, — Cal. —, 183 Pac. 789.

⁷⁹ Chapman v. First Nat. Bank, — Wyo. —, 181 Pac. 360, notes and mortgage.

⁸⁰ Caddy Oil Co. v. Sommer, 186 Ky. 843, 218 S. W. 288.

⁸¹ Mitchell Street State Bank v. Schaefer, 169 Wis. 543, 173 N. W. 330.

⁸² First Nat. Bank of Sweetwater, Texas v. Rust, 257 Fed. 29.

⁸³ Rosenberger v. H. E. Wilcox Motor Co., — Minn. —, 177 N. W. 625.

⁸⁴ Palmer-Haworth Logging Co. v. Henderson, 90 Ore. 192, 174 Pac. 531.

sentations of officers of a bank, inducing the execution of a note to the bank, are imputable to the bank.⁸⁵

A bank is not bound by the false statement of an officer that the bank has been merged with another, since a merger is not in the usual course of business.⁸⁶ A letter written by a corporate officer after an assignment for benefit of creditors is not admissible against the corporation to show an independent acknowledgment by the corporation of the existence of a corporate debt.⁸⁷

§ 2168. Statements of particular officers or agents—Directors. Statements of one director are not binding on the others⁸⁸ nor on the board of directors as a whole.⁸⁹ For instance, directors are not bound by statements of a codirector who is president that money furnished by the directors to the company was a donation and not a loan.⁹⁰

§ 2169. — President. Representations of the president are not binding on the corporation in many instances.⁹¹ For instance, statements by the president of a bank as to a matter vested by statute exclusively in the directors are not binding on the bank.⁹² So the president has no implied power to bind the corporation by declarations as to boundaries; but it is otherwise where he is in general charge of the lands and actively looking after the establishment of the boundaries.⁹³ Statements by the president at the office of the corporation, while in charge of the corporate business and in the course of negotiations within the scope of his general authority, are binding on the corporation.⁹⁴

⁸⁵ *Brady v. Cobbs*, — Tex. Civ. App. —, 211 S. W. 802.

⁸⁶ *Drovers' & Mechanics' Nat. Bank v. First Nat. Bank*, 260 Fed. 9.

⁸⁷ *Hurley-Mason Co. v. Pacific Commissary Co.*, — Wash. —, 191 Pac. 624.

⁸⁸ *Schuster Bros. v. Davis Bros.*, 185 Iowa 143, 170 N. W. 292.

⁸⁹ *Reuter v. Nixon State Bank*, — Tex. Civ. App. —, 206 S. W. 715.

⁹⁰ *Andrews v. Cosmopolitan Bank*, 183 N. Y. App. Div. 787, 171 N. Y. Supp. 875, rev'g on other grounds 101 N. Y. Misc. 672, 167 N. Y. Supp. 935.

⁹¹ See *Ichelson v. S. Schlein & Sons*, 103 N. Y. Misc. 673, 171 N. Y. Supp. 2.

⁹² *Conway v. First Nat. Bank*, 256 Fed. 277.

⁹³ *Blacksburg Min. & Mfg. Co. v. Bell*, 125 Va. 565, 100 S. E. 806.

⁹⁴ *Rosenberger v. H. E. Wilcox*

The cashier and president of a bank have no authority to make representations to a prospective purchaser of stock of the bank, as to the condition of the bank and the value of the stock.⁹⁵

A director is not bound personally by the representations of the president of the corporation.⁹⁶

§ 2172. — General manager.⁹⁷ A general manager has power to represent that certain indebtedness of the corporation exists, in order to obtain a loan.⁹⁸ Since merger of a corporation with another is not in the usual course of business of a corporation, the corporation is not bound by the false statement of a vice president or other official in charge of its current business that there has been a merger and assumption of liabilities of the absorbed corporation.⁹⁹

§ 2173. — Cashier. Declarations of a cashier in connection with a loan are binding on the bank.¹

§ 2174. — Miscellaneous agents. Agents to whom the entire subject of making sales of land was left by the corporation have ostensible authority to represent that certain land within the subdivision was to be used as a public street.²

Declarations of a foreman are binding on the corporation only when they were made in the course of, or in connection with, those duties which he has been authorized to perform.³

Motor Co., — Minn. —, 177 N. W. 625, citing 3 Fletcher Cyc. Corp., § 2160.

⁹⁵ Farmers' State Guaranty Bank v. Cromwell, — Okla. —, 173 Pac. 826.

⁹⁶ Andrews v. Cosmopolitan Bank, 183 N. Y. App. Div. 787, 171 N. Y. Supp. 875.

⁹⁷ See generally Porterfield v. American Surety Co., 201 Mo. App. 8, 210 S. W. 119.

⁹⁸ Hartley v. Ault Woodenware Co., 82 W. Va. 780, 97 S. E. 137.

⁹⁹ Drivers' & Mechanics' Nat. Bank v. First Nat. Bank, 260 Fed. 9.

¹ Mitchell Street State Bank v. Schaefer, 168 Wis. 543, 173 N. W. 330.

² City of Venice v. Short Line Beach Land Co., — Cal. —, 181 Pac. 658.

³ Craig's Adm'x v. Kentucky Utilities Co., 183 Ky. 274, 209 S. W. 33.

XXII. RATIFICATION AND ESTOPPEL

§ 2177. General considerations.⁴ A public service company which occupies property as a tenant or by permission is subject to the same rules as to estoppel, etc., as private persons.⁵

§ 2178. Statement of general rule. Unauthorized acts of corporate officers or employees may be validated by ratification by the corporation.⁶ The general doctrine of estoppel in pais operates against corporations in like manner as against natural persons.⁷ Estoppel by deed applies to corporations as well as to persons.⁸

A report of an officer to his corporation is not an account stated, and the approval of the report does not estop the corporation to deny its accuracy.⁹

§ 2181. Ultra vires acts. There can be no ratification of an act which an officer is forbidden to do by statute and which the statute declares to be "null and void."¹⁰ Acts of a cashier of a bank in violation of a statute cannot be validated by ratification of the directors.¹¹

§ 2182. Knowledge as element of ratification—General rule. Ratification, to be effectual, must have been made with a full knowledge of all material facts.¹² Ratification of dealings be-

⁴ Ratification distinguished from estoppel, see *Depot Realty Syndicate v. Enterprise Brewing Co.*, 87 Ore. 560, L. R. A. 1918 C 1001, 171 Pac. 223.

⁵ *Western U. Tel. Co. v. Louisville & N. R. Co.*, 250 Fed. 199.

⁶ *Georgia Casualty Co. v. Massey*, 201 Ala. 601, 79 So. 33; *Rowland v. Progressive Inv. Co.*, — Mo. App. —, 202 S. W. 257; *Lawrence Coal Co. v. Shanklin*, — N. M. —, 183 Pac. 435.

⁷ *Ravinia State Bank v. Kirkpatrick*, — S. D. —, 173 N. W. 863.

The doctrine of equitable estoppel operates against corporations in like manner as against

natural persons, and the estoppel by acquiescence of the cashier and manager of a bank operates as an estoppel against the bank. *Ravinia State Bank v. Kirkpatrick*, — S. D. —, 173 N. W. 863.

⁸ *Hartley v. Ault Woodenware Co.*, 82 W. Va. 780, 97 S. E. 137.

⁹ *Stagg v. Kansas Free Fair Ass'n*, 105 Kan. 600, 8 A. L. R. 478, 185 Pac. 893.

¹⁰ *Bank of Kirksville v. Sloop*, 198 Mo. App. 225, 200 S. W. 72.

¹¹ *Taylor v. Fuqua*, — Mo. App. —, 219 S. W. 971; *Bank of Kirksville v. Sloop*, 198 Mo. App. 225, 200 S. W. 72.

¹² *Emerson v. Fisher*, 246 Fed.

tween a director and the corporation by acquiescence alone must be based on knowledge plus opportunity to act.¹³ However, ratification of a contract is binding although the corporation had no knowledge as to the commissions agreed to be paid.¹⁴

§ 2185. — Knowledge of officer or agent as imputable to corporation. While knowledge of the affairs of a bank by the directors will be presumed in favor of an innocent third person, no such presumption is indulged in favor of the president who is himself a director.¹⁵

§ 2186. Who may ratify—General rules. Employment of an attorney may be ratified by the directors or at a stockholders' meeting.¹⁶

§ 2187. — Ratification of one's own acts. A corporate officer cannot ratify his own unauthorized act.¹⁷ For instance, directors cannot ratify their own violations of duty although the guilty directors constitute a majority of the directors or of the stockholders.¹⁸ Likewise, a contract made by promoters cannot be ratified by the same persons as directors after creation of the corporation.¹⁹ So the president cannot himself ratify his own unauthorized act.²⁰

§ 2188. — Directors. Unauthorized acts of the president of a corporation may be ratified by the board of directors if the

642; *Caddy Oil Co. v. Sommer*, 186 Ky. 843, 218 S. W. 288; *First State Bank v. Lang*, — Mont. —, 174 Pac. 597; *Fields v. Victor Building & Loan Co.*, — Okla. —, 175 Pac. 529; *Guaranty Bank & Trust Co. v. Beaumont Cadillac Co.*, — Tex. Civ. App. —, 218 S. W. 638; *Citizens' Nat. Bank v. Blizzard*, 80 W. Va. 511, L. R. A. 1918 A 129, 93 S. E. 338.

¹³ *Jordan v. Jordan Co.*, — Conn. —, 109 Atl. 181.

¹⁴ *Conservation Co. v. Stimpson*, — Md. —, 110 Atl. 495.

¹⁵ *First State Bank v. Lang*, — Mont. —, 174 Pac. 597.

¹⁶ *Ney v. Eastern Iowa Tel. Co.*, 185 Iowa 610, 171 N. W. 26.

¹⁷ *Sheatz v. Markley*, 249 Fed. 315.

¹⁸ *Farwell v. Pyle-National Elec. Headlight Co.*, 289 Ill. 157, 10 A. L. R. 363, 124 N. E. 449, aff'g 212 Ill. App. 450.

¹⁹ *Ennis v. New World Life Ins. Co.*, 97 Wash. 122, 165 Pac. 1091.

²⁰ *Hoffman v. M. Gottstein Inv. Co.*, 101 Wash. 428, 172 Pac. 573.

acts are within the powers of the directors.²¹ Acts of a minority of the directors may be ratified by the other directors.²² So conduct of individual directors may amount to ratification.²³ In California, ratification may be by the knowledge, approval and consent of a majority of the board of directors acting individually and informally.²⁴

§ 2189. — Officers or agents other than directors. A general manager has power to ratify a contract which is within the scope of his authority to make, when such contract is made by an unauthorized person.²⁵

§ 2190. — Stockholders. Acts of officers, where unauthorized, may be ratified by the stockholders,²⁶ but not where against public policy or expressly prohibited by statute.²⁷ Where a contract is made for the corporation by its manager and ratified by the only other real stockholder, it is no defense that the contract was made without observing the formal requisites required by the charter.²⁸ It has been held that ratification of acts of directors by acquiescence of the stockholders, after being given written notice of the acts of the directors, is binding on the corporation;²⁹ but it is also held that mere consent or silence on the part of stockholders does not operate as a ratification or an estoppel.³⁰ A stockholder who consents to a corporate act is afterwards estopped to attack it.³¹

²¹ *Caddy Oil Co. v. Sommer*, 186 Ky. 843, 218 S. W. 288.

²² *Geisenberger & Friedler v. Robert York & Co.*, 262 Fed. 739.

²³ *Dickinson v. Citizens' Ice & Fuel Co.*, 139 Minn. 201, 165 N. W. 1056.

²⁴ *Countryman v. California Trona Co.*, — Cal. —, 170 Pac. 1069.

²⁵ *Braman, Dow & Co. v. Kennebec Gas & Fuel Co.*, 117 Me. 291, 104 Atl. 3.

²⁶ *West Side Irrigation Co. v. United States*, 246 Fed. 212; *Bunn*

v. City of Laredo, — Tex. Civ. App. —, 213 S. W. 320.

²⁷ *Martindale v. DeKay*, 101 N. Y. Misc. 728, 166 N. Y. Supp. 405.

²⁸ *Commercial Security Co. v. Modesto Drug Co.*, — Cal. App. —, 184 Pac. 964.

²⁹ *Grice v. Anderson*, 109 S. C. 388, 96 S. E. 222.

³⁰ *Southern California Home Builders v. Young*, — Cal. App. —, 188 Pac. 586.

³¹ *Fish v. Harrison*, 87 N. J. Eq. 103, 100 Atl. 185.

§ 2193. How ratification may be effected in general—Express and implied. Ratification may be informal.³² It need not be by formal vote.³³ The assent of a corporation to acts done on its account may be inferred in the same manner that the assent of a natural person may be.³⁴

§ 2195. Silence or acquiescence as ratification—General rules. Acquiescence by silence may amount to ratification as well as affirmative action.³⁵ Acquiescence may rest on the principle of ratification or upon the principle of estoppel.³⁶

§ 2196. — Application of rules. Contracts of employment may be ratified by silence with knowledge of the rendition of such services.³⁷ A church corporation may be estopped to deny the authority of an officer to hire a broker to sell church land, by knowledge of the contract and of expenditures by the broker.³⁸ Silence and inaction of officers and stockholders amounts to a ratification of payments by a corporate officer of his own debts by corporate checks.³⁹ Silence of one who is cashier and manager of a bank, sufficient to estop him as an individual, works an estoppel against the corporation.⁴⁰ Want of power of an officer to execute a chattel mortgage may be

³² *Security State Bank v. Fischer*, 38 N. D. 132, 164 N. W. 326.

³³ *In re National Piano Co.*, 252 Fed. 950.

³⁴ *Harwood v. Ft. Worth Nat. Bank*, — Tex. Civ. App. —, 205 S. W. 484.

³⁵ *Atherton v. Beaman*, 256 Fed. 871, 875; *Mobile Towing & Wrecking Co. v. First Nat. Bank of Lakeland, Florida*, 201 Ala. 419, 78 So. 797; *Bacon v. Bankers' Trust & Savings Bank*, 143 Minn. 318, 173 N. W. 719; *Depot Realty Syndicate v. Enterprise Brewing Co.*, 87 Ore. 560, L. R. A. 1918 C 1001, 170 Pac. 294; *Harwood v. Ft. Worth Nat. Bank*, — Tex. Civ. App. —, 205 S. W. 484.

Failure to disaffirm after knowledge constitutes ratification. *Citizens' Saving Trust Co. v. Independent Lumber Co.*, — Neb. —, 178 N. W. 270.

³⁶ *In re Grocers' Baking Co.*, 266 Fed. 900, citing 4 *Fletcher Cyc. Corp.*, § 2195.

³⁷ *Baker v. Brown & Hackney*, — Ark. —, 215 S. W. 578; *Bacon v. Bankers' Trust & Savings Bank*, 143 Minn. 318, 173 N. W. 719.

³⁸ *Stablein v. Hutterische Gemeinde*, — S. D. —, 177 N. W. 810.

³⁹ *Atherton v. Beaman*, 256 Fed. 871.

⁴⁰ *Ravinia State Bank v. Kirkpatrick*, — S. D. —, 173 N. W. 863.

cured by ratification of the mortgage by the corporation by approval and failure to return the proceeds.⁴¹

§ 2197. — Retention of agent as ratification. Permitting an attorney to continue as such for the corporation without objection or inquiry ratifies his unauthorized employment by the general manager.⁴²

§ 2198. — Time within which to disaffirm. A corporation cannot disavow acts of its officers unless it promptly returns or tenders back the benefits received.⁴³

§ 2199. Acceptance and retention of benefits as implied ratification. Acceptance of benefits with knowledge is an implied ratification.⁴⁴ Acceptance of benefits of a contract estops the corporation to deny the authority of the contracting officer.⁴⁵ Authority or ratification may be inferred where the corporation receives and retains property by virtue of the contract.⁴⁶ For instance, acceptance of services rendered with full knowledge

⁴¹ *In re Grocers' Baking Co.*, 266 Fed. 900.

⁴² *Countryman v. California Trona Co.*, — Cal. —, 170 Pac. 1069.

⁴³ *Magnolia Compress & Warehouse Co. v. St. Louis Cash Register Co.*, — Mo. App. —, 210 S. W. 125.

⁴⁴ *Standard Roller Bearing Co. v. Hess-Bright Mfg. Co.*, 264 Fed. 516; *Wilson v. Davis*, 138 Ark. 111, 211 S. W. 152; *Ebner v. West Hollywood Transfer Co.*, — Cal. App. —, 187 Pac. 114; *Lang v. Pacific Brewing & Malting Co.*, — Cal. App. —, 187 Pac. 81; *Commercial Security Co. v. Modesto Drug Co.*, — Cal. App. —, 184 Pac. 964; *Hammitt v. Virginia Min. Co.*, 32 Idaho 245, 181 Pac. 336; *Bertholf v. Fisk*, 182 Iowa 1308, 166 N. W. 713; *Gasser v. Great Northern Ins. Co.*, — Minn. —, 176 N. W. 484; *Dickinson v. Citizens'*

Ice & Fuel Co., 139 Minn. 201, 165 N. W. 1056; *Morris v. Basnight*, 179 N. C. 298, 102 S. E. 389; *McBride v. Western Pennsylvania Paper Co.*, 263 Pa. 345, 106 Atl. 720; *Southern Amusement Co. v. Ferrell-Bledsoe Furniture Co.*, 125 Va. 429, 99 S. E. 716; *Chafin v. Main Island Creek Coal Co.*, — W. Va. —, 102 S. E. 291; *Stevens v. Merchants Bank of Canada*, 42 Dom. L. Rep. (Can.) 171.

Corporate obligations assumed by bank officers, as where they execute notes personally to secure money for the bank, are binding on the corporation which accepts the benefits thereof. *Jensen v. Sawyer State Bank*, — N. D. —, 173 N. W. 162.

⁴⁵ *Butler v. Solano Land Co.*, — Cal. App. —, 188 Pac. 1019.

⁴⁶ *In re National Piano Co.*, 252 Fed. 950.

of the contract under which rendered is a ratification of such contract.⁴⁷ So a corporation cannot repudiate a lease, on the ground of want of authority of its agent to execute it, where it has enjoyed its benefits for many years.⁴⁸ A corporation cannot deny the authority of its president to execute a note, when sued thereon, where it retains the property for which the note was given.⁴⁹ Where money procured by a transfer of corporate paper by the president has been turned over to and retained by the corporation, the transfer cannot be attacked by the corporation on the ground that the president had been deprived of power to make such a transfer by resolution of the directors.⁵⁰ Receipt and retention by the company of the benefit of loans to it estops it to deny the authority of its agents to obtain the loan.⁵¹ The rule also applies to the acceptance of the benefits of a guaranty.⁵²

⁴⁷ *Chard v. Ryan-Parker Const. Co.*, 182 N. Y. App. Div. 455, 169 N. Y. Supp. 622; *Rainbow Oil & Gas Co. v. Barton*, — Okla. —, 173 Pac. 1135; *Rae v. Heilig Theater Co.*, 94 Ore. 408, 185 Pac. 909.

Acceptance of benefits is ratification of employment of manager by the president of the corporation. *Mutual Oil Co. v. Hills*, 248 Fed. 257.

The corporation is liable for the reasonable value of the services of attorneys rendered with knowledge of the officers in charge of the corporation. In *re United States Molybdenum Co.*, 255 Fed. 790.

A corporation is liable for services rendered and accepted by it although there is no express contract of employment or the employment was by an unauthorized officer. *Brooks v. Geo. Q. Cannon Ass'n*, — Utah —, 178 Pac. 589.

An insurance corporation is liable for reasonable fees for services in adjusting claims against

the company without regard to whether the employment was by an authorized officer or agent, where the controlling officers had knowledge of the services and the corporation accepted the benefits thereof. *Bostwick v. Mutual Life Ins. Co. of New York*, 251 Fed. 36.

⁴⁸ *Lang v. Pacific Brewing & Malting Co.*, — Cal. App. —, 187 Pac. 81.

⁴⁹ *Ebner v. West Hollywood Transfer Co.*, — Cal. App. —, 187 Pac. 114; *Phillips v. Interstate Land Co.*, 176 N. C. 514, 97 S. E. 417.

It is no defense to a corporate note that it was not executed by the proper officer where the corporation has received the benefits of the note. *Scouton v. Stony Brook Lumber Co.*, 261 Pa. 241, 7 A. L. R. 1433, 104 Atl. 548.

⁵⁰ *Cardwell v. Garrison*, 179 N. C. 476, 103 S. E. 3.

⁵¹ *Hartley v. Ault Woodenware Co.*, 82 W. Va. 780, 97 S. E. 137.

⁵² *Armour & Co. v. R. Rosenberg & Sons Co.*, 36 Cal. App. 773, 173

§ 2200. Recognition or adoption of act or contract by affirmative acts as ratification—In general. Acceptance of rent is a ratification of a lease.⁵³

§ 2201. — Payments by corporation. Payment on a note by a corporation is a ratification of its unauthorized execution.⁵⁴

§ 2203. Evidence to show ratification—In general. Ratification need not be shown by the corporate minutes.⁵⁵

§ 2204. — Presumptions. The assent of the corporation to a dedication by its head officer will be assumed.⁵⁶

§ 2206. Question for jury. Ratification is generally a question of fact for the jury.⁵⁷

§ 2207. Effect of ratification—General rules. Ratification relates back to the time of the contract ratified and is equivalent to original authority.⁵⁸ A ratification by stockholders of acts of directors in conveying the corporate assets to another company relates back to the date of the directors' contract, and has the same effect as if the conveyance had been originally authorized by the stockholders.⁵⁹ The right to avoid a contract because made by an unauthorized officer is waived where the contract has been ratified by the corporation.⁶⁰ Ratification

Pac. 404; *Weiss v. Fred Bender Store Fixture Co.*, 207 Ill. App. 72.

⁵³ *Commercial Trust Co. v. L. Wertheim Coal & Coke Co.*, 88 N. J. Eq. 143, 102 Atl. 448.

⁵⁴ *California Nat. Supply Co. v. Flack*, — Cal. —, 190 Pac. 634.

⁵⁵ *Wright v. Barnard*, 248 Fed. 756.

⁵⁶ *Duke Land & Improvement Co. v. Murphy*, 179 N. C. 133, 101 S. E. 497.

⁵⁷ *Coleman v. Northwestern Mut. Life Ins. Co.*, 273 Mo. 620, 201 S. W. 544. See *Joseph v. National Bank*, — Utah —, 173 Pac. 897.

⁵⁸ *In re Grocers' Baking Co.*, 266 Fed. 900, quoting 4 *Fletcher Cyc. Corp.*, § 2207; *Union Oil Co. v. Pacific Surety Co.*, — Cal. —, 187 Pac. 14; *Commercial Bank & Trust Co. v. Beach*, — Colo. —, 180 Pac. 982; *Emmett v. Astoria Marine Iron Works*, — Ore. —, 192 Pac. 1113; *Goldstein v. Union Nat. Bank*, 109 Tex. 555, 213 S. W. 584; *Oberman v. Red Rock Fuel Co.*, 83 W. Va. 531, 99 S. E. 66.

⁵⁹ *Buck v. Gimon*, 201 Ala. 619, 79 So. 51.

⁶⁰ *Foster v. C. G. Howes Co.*, 230 Mass. 43, 119 N. E. 356.

after knowledge prevents a corporation from defending an action on a guaranty on the ground that its vice president had no authority to execute the guaranty.⁶¹ Ratification of a contract by acceptance of its benefits is a ratification of all the terms of the contract although the corporation has no actual knowledge of such terms.⁶² Acquiescence of original holders of stock in illegal acts of the directors does not bind a subsequent holder to submission to all future acts of the same character.⁶³

§ 2208. — Ratification of part. A corporation cannot ratify in part and repudiate in part.⁶⁴ A corporation cannot accept the benefits and repudiate the obligations of a stock deal made by its president in his own name but for the benefit of the corporation.⁶⁵

§ 2210. Estoppel of officers, agents or stockholders. A director who makes a contract cannot himself afterwards attack it on the ground that it was not authorized by two-thirds of the stockholders as required by statute.⁶⁶ So the president of a corporation who executes a deed in its behalf, with warranty of title, is estopped to set up an adverse title.⁶⁷ Likewise, corporate officers who sign notes cannot afterwards attack them as fraudulently given.⁶⁸ Illegal or ineffective acts of a corporate officer on behalf of the corporation will not estop a mere stockholder thereof, who has no notice of them until after third persons have acted upon them, from enforcing a valid vendor's lien against the corporation.⁶⁹ A person may by his acts be estopped to claim title to stock.⁷⁰

⁶¹ *Standard Brewery v. Creedon*, 283 Ill. 474, 119 N. E. 581, aff'g 204 Ill. App. 431.

⁶² *Meeuwesen v. Clough & Warren Co.*, 207 Mich. 697, 175 N. W. 408.

⁶³ *Odell v. Wells*, 183 N. Y. App. Div. 242, 171 N. Y. Supp. 345.

⁶⁴ *Rocky River Development Co. v. German-American Brewing Co.*, 193 N. Y. App. Div. 197, 184 N. Y. Supp. 155.

⁶⁵ *Swartz v. Burr*, — Cal. App. —, 185 Pac. 411.

⁶⁶ *Amos v. Continental Trust Co.*, 22 Ga. App. 348, 95 S. E. 1025.

⁶⁷ *Edwards v. Sarasota Venice Co.*, 246 Fed. 773.

⁶⁸ *Hille v. Evans*, — Colo. —, 187 Pac. 315.

⁶⁹ *Rader v. Star Mill & Elevator Co.*, 258 Fed. 599.

⁷⁰ See *Farish v. Beebe*, — Ariz. —, 179 Pac. 51.

XXIII. NOTICE TO OR KNOWLEDGE OF OFFICERS OR AGENTS AS
CHARGEABLE TO CORPORATION

§ 2215. General statement of rule as applied to corporations. Knowledge of a corporate officer or agent, in the course of his employment, and as to matters which are within the scope of his authority, is imputable to the corporation.⁷¹

§ 2218. Knowledge obtained outside scope of duties or while not acting officially—Statement of rule. Knowledge of a corporate officer coming to him through his private transactions outside of his official duties is not imputable to the corporation.⁷² In other words, knowledge derived by an officer as an individual and not as an officer cannot be imputed to the corporation.⁷³ Notice to an officer is imputable to the corporation only when the officer was authorized to act for the corporation in regard thereto.⁷⁴ Thus, an action against the president of a corporation individually is not of itself notice to the corporation of the action.⁷⁵ A corporation is not chargeable with knowledge of facts which become known to its agent, unless the agent in the line of his duty ought and would reasonably be expected to communicate the knowledge to his principal.⁷⁶

⁷¹ *Corrigan v. Bobbs-Merrill Co.*, 228 N. Y. 58, 10 A. L. R. 662, 126 N. E. 260, rev'g on other grounds 182 N. Y. App. Div. 919, 169 N. Y. Supp. 1089.

⁷² *Sims v. Southeast Missouri Trust Co.*, 140 Ark. 365, 215 S. W. 671; *Alsabrooks v. Bank of Sparta*, 22 Ga. App. 693, 97 S. E. 111; *Corrigan v. Bobbs-Merrill Co.*, 228 N. Y. 58, 10 A. L. R. 662, 126 N. E. 260.

⁷³ *Coleman v. Shortsville Wheel Co.*, 257 Fed. 591; *Keyworth v. Nevada Packard Mines Co.*, — Nev. —, 186 Pac. 1110.

Knowledge of its president is not knowledge of the bank where acquired in his individual capacity and not as president. *Farmers' Bank of Grandview v. Ozias*, — Mo. App. —, 209 S. W. 580.

Knowledge of a timekeeper and shipping clerk having no charge of operations except as to keeping the records and looking after shipments, as to the place where a truck driver was keeping his truck, is not imputed to the corporation, since not acquired within the scope of his authority. *United Disposal & Recovery Co. v. Industrial Commission*, 291 Ill. 480, 126 N. E. 183, citing *Fletcher Cyc. Corp.*, § 2214.

⁷⁴ *Union Warehouse Co. v. Roper*, 21 Ga. App. 182, 94 S. E. 74.

⁷⁵ *O'Donnell v. Braun & Kohn*, 167 N. Y. Supp. 914.

⁷⁶ *Elgin, J. & E. R. Co. v. United States*, 253 Fed. 907, 912, holding particular instruction too broad; *Corrigan v. Bobbs-Merrill*

The fact that the cashier who acted for a bank in making a loan was the same individual who sold an automobile to the borrower, and as such seller received the proceeds of the loan, does not make the bank liable for breach of the seller's warranty because the cashier had knowledge of the terms of the warranty.⁷⁷

§ 2221. — Qualification of rule where agent subsequently acts in regard to matter concerning which he obtained knowledge outside the scope of his duties. In Minnesota the rule is, at least as to banks, that "a bank is chargeable with knowledge possessed by its active officer pertaining to transactions within the scope of the bank's business, even though such knowledge is acquired in another transaction, if it appears that the knowledge is actually present in his mind while he is acting for the bank."⁷⁸

§ 2227. Constructive notice to officer or agent as equivalent to actual knowledge or notice. A bank is not chargeable with knowledge of facts which at best could only be presumed to be known to one of its officers merely because such officer is also an officer of another corporation.⁷⁹

§ 2230. Applicability of rules to particular corporations. Knowledge of an officer of a bank as to the terms of a bank loan made by him ordinarily is chargeable to the bank.⁸⁰

§ 2231. Application of general rules to particular officers, agents or other persons—In general.⁸¹ A corporation is chargeable with notice possessed by its incorporators shortly before the creation of the corporation.⁸² Knowledge of the vice presi-

Co., 228 N. Y. 58, 10 A. L. R. 662, 126 N. E. 260.

⁷⁷ Brown v. Bank of Covington, — Ga. App. —, 101 S. E. 196.

⁷⁸ State Bank of Morton v. Adams, 142 Minn. 63, 170 N. W. 925.

⁷⁹ Muschelwicz v. Tidrick, 40 S. D. 435, 167 N. W. 499.

⁸⁰ Goldstein v. Union Nat. Bank, 109 Tex. 555, 213 S. W. 584.

⁸¹ Knowledge of assistant secretary held knowledge of the corporation. Trust Co. of St. Louis County v. Phoenix Ins. Co. of Hartford, Connecticut, — Mo. App. —, 210 S. W. 98.

⁸² Walla Walla Oil, Gas & Pipe Line Co. v. Vallentine, 103 Wash. 359, 174 Pac. 980.

dent as to fraudulent procurement of a patent to land is imputable to the purchasing corporation.⁸³ Knowledge of the treasurer as to existence of corporate debts is not imputable to the corporation so as to make fraudulent a transfer of the corporate assets by the sole stockholder without actual knowledge of any corporate indebtedness.⁸⁴

§ 2232. — Director or directors. Knowledge of a director is imputed to the corporation,⁸⁵ and notice to directors is notice to the corporation.⁸⁶ Thus, knowledge of a director who verified the petition on which an attachment was issued, as to disposal of property with intent to defraud the corporation, is imputable to the corporation.⁸⁷ But notice to a director merely as an individual and not in connection with any transaction as to which the director had authority is not notice to the corporation.⁸⁸

§ 2235. — President. Knowledge of the president of a bank, coming to him in due course of his duties as such officer, is imputable to the bank.⁸⁹ A corporation is presumed to know of a contract executed by its president, although in his own name, where it receives the consideration.⁹⁰ Knowledge of the president of a corporation in regard to a corporate agreement is imputable to the corporation where he represented the corporation in making such agreement.⁹¹

§ 2236. — Cashier and inferior officers or agents of bank. Knowledge of the cashier of a bank obtained in promotion of its legitimate business, and at a time when he was not acting in hostility to the bank, is imputable to the bank.⁹² Knowledge

⁸³ *United States v. Routt County Coal Co.*, 248 Fed. 485.

⁸⁴ *In re M. S. Fersko, Inc.*, 250 Fed. 357.

⁸⁵ *Botna Valley State Bank v. Greig*, 182 Iowa 662, 166 N. W. 104.

⁸⁶ *Watt v. German Sav. Bank*, 183 Iowa 346, 165 N. W. 897.

⁸⁷ *Botna Valley State Bank v. Greig*, 182 Iowa 662, 166 N. W. 104.

⁸⁸ *Western Securities Co. v. Silver King Consol. Min. Co.*, — Utah —, 192 Pac. 664.

⁸⁹ *Pollman v. Curtice*, 255 Fed. 628; *Merchants' Nat. Bank v. Marden, Orth & Hastings Co.*, — Mass. —, 125 N. E. 384.

⁹⁰ *Swartz v. Burr*, — Cal. App. —, 185 Pac. 411.

⁹¹ *Gila Land & Water Co. v. Page*, — Ariz. —, 181 Pac. 457.

⁹² *Tescene v. Iowa State Bank*,

of the trust character of a deposit is imputed to a bank by knowledge of the cashier in obtaining the deposit.⁹³

§ 2233. — Members or stockholders. Notice to all the stockholders is notice to the corporation,⁹⁴ but knowledge of a member of a church is not imputed to the corporation.⁹⁵

§ 2239. Application of rules to knowledge of particular facts. If a corporation has creditors, to the knowledge of any of its officials or agents, by whose knowledge it would in ordinary business affairs be bound, such knowledge is imputed to it, and this applies to preferential payments to a creditor officer, as an act of bankruptcy.⁹⁶

§ 2243. Exception to general rule where officer or agent adversely interested—Statement of exception. Knowledge of an officer is not imputed to the corporation where in relation to a transaction in which he is interested adversely to the corporation.⁹⁷

§ 2244. — Reasons for exception. After reviewing at length the decisions and reasons therefor relating to notice to a corporate officer or agent as notice to the corporation, where the interests of the latter are adverse to the corporation, the Supreme Court of Texas, in a carefully prepared and scholarly opinion by Justice Hawkins, lays down what it deems to be

— Iowa —, 173 N. W. 918, applying rule to knowledge of trust character of deposit in bank.

⁹³ *Tesene v. Iowa State Bank*, — Iowa —, 173 N. W. 918.

⁹⁴ *Wallace v. Eclipse Pocahontas Coal Co.*, 83 W. Va. 321, 98 S. E. 293.

⁹⁵ *Concordia Fire Ins. Co. v. Waterford*, — Ark. —, 224 S. W. 953.

⁹⁶ *In re Boston-West Africa Trading Co.*, 255 Fed. 924.

⁹⁷ *In re M. S. Fersko, Inc.*, 250 Fed. 357; *Western Securities Co. v. Silver King Consol. Min. Co.*, — Utah —, 192 Pac. 664, quoting

4 *Fletcher Cyc. Corp.*, § 2243; *Citizens' Nat. Bank v. Blizzard*, 80 W. Va. 511, L. R. A. 1918 A 129, 93 S. E. 338.

Adverse interests as affecting imputation to corporation of knowledge of officer or agent are fully discussed in *Goldstein v. Union Nat. Bank*, 109 Tex. 555, 213 S. W. 584.

Where the interest of the officer selling is adverse to that of the purchasing corporation, notice to the officer is not notice to the corporation. *Reed v. West Loan & Trust Co.*, 22 Ga. App. 397, 95 S. E. 1002.

the better rule as follows: "The true test, as to notice, in cases of this character, is, we think, not whether there is some slight adverse interest existing in the agent, although, to much greater extent, his individual interests in the transaction are entirely consistent with the interests of his principal, but whether, in the premises, and under all the circumstances of the particular case, the agent's interests are so incompatible with the interests of his principal as practically to destroy the agency or to render it reasonably probable that an ordinary person, in the agent's position, under such circumstances, will neither act upon his so acquired knowledge, nor disclose that knowledge to his principal, but, because of such incompatibility in interests, will withhold such knowledge from the principal."⁹⁸

§ 2247. — Illustrations and applications of exception. Knowledge of the president is not imputable to the corporation where it is to his interest to conceal such knowledge.⁹⁹ For instance, knowledge of a bank president is not imputable to the bank where his interests in connection therewith conflicted with those of the bank.¹ So where the president of a bank represents the other contracting party, in a contract with the bank, his knowledge is not imputed to the bank.² Where a president of a bank gave it a deed to secure his debt to it, the bank was not chargeable with his knowledge of a prior unrecorded bond for title given by the president to a third person.³ A bank is not chargeable with knowledge of its cashier in connection with his acts adverse to the bank.⁴ Knowledge of a bank vice president as to the illegality of the consideration of a note assigned by him to the bank is not imputed to the bank.⁵

§ 2248. — Where same person is agent both of corporation and of other party to transaction: Interlocking officers.⁶ The

⁹⁸ Goldstein v. Union Nat. Bank, 109 Tex. 555, 213 S. W. 584.

⁹⁹ Blum v. Allen, 145 La. 71, 81 So. 760.

¹ Greer v. Levee Dist. No. 3, Conway County, 140 Ark. 60, 215 S. W. 171.

² Kipp v. Welsh, 141 Minn. 291, 170 N. W. 222.

³ Cooper v. Robertson Inv. Co., 117 Miss. 108, 77 So. 953.

⁴ Holmes v. Uvalde Nat. Bank, — Tex. Civ. App. —, 222 S. W. 640.

⁵ State v. Emery, — Okla. —, 174 Pac. 770.

⁶ Knowledge of common agent or officer as imputed to corporation, see California Nat. Supply

rule that knowledge of a corporate officer will not be imputed to his corporation when he is acting in his own interest does not apply when the same person acts for both corporations.⁷ Notice to a corporation is imputed to another corporation having the same executive officers, the same claim department, the same counsel, and practically the same directors.⁸ Where the same person was president of a corporation which transferred all its assets to another corporation, and also of the latter corporation, the grantee corporation was chargeable with notice of the liability of the grantor corporation to one injured by its negligence.⁹ However, knowledge of an officer merely because he is also an officer of another corporation is not imputed to the first corporation.¹⁰ So knowledge of a director as to the infirmity of a note taken by the corporation is not imputable to other corporations of which he is also director where they afterwards purchased the note.¹¹

§ 2250. — Application of exception to independent frauds against the corporation. Knowledge of the fraud of a director while acting for himself is not imputable to the corporation.¹² Knowledge of the president of a bank is not imputable to the bank where obtained while acting fraudulently towards the bank.¹³

§ 2251. — Qualification of exception where interested officer or agent is sole representative of corporation to whom notice is sought to be imputed.¹⁴ The exception does not apply when the transaction on behalf of the corporation, to which notice is sought to be imputed, is intrusted "solely" to the officer or

Co. v. Black, — Cal. App. —, 191 Pac. 715.

⁷ Manchester Nat. Bank v. Herndon, 181 Ky. 117, 203 S. W. 1055.

⁸ Johnson v. United Rys. Co., — Mo. —, 219 S. W. 38. See also Wilkins-Ricks Co. v. Welch, 179 N. C. 266, 102 S. E. 316.

⁹ Burnwell Coal Co. v. Setzer, — Ala. —, 83 So. 139.

¹⁰ Muschelwicz v. Tidrick, 40 S. D. 435, 167 N. W. 499.

¹¹ Sims v. Southeast Missouri

Trust Co., 140 Ark. 365, 215 S. W. 671.

¹² Keyworth v. Nevada Packard Mines Co., — Nev. —, 186 Pac. 1110.

¹³ Interstate Nat. Bank v. Yates Center Nat. Bank, 245 Fed. 294.

¹⁴ For a valuable discussion of the grounds for the "sole representative" exception, see Goldstein v. Union Nat. Bank, 109 Tex. 555, 213 S. W. 584.

agent having the knowledge.¹⁵ The Texas Supreme Court, in a valuable decision, says, in regard to this "sole representative" exception, that "this court is not committed to that doctrine as a general rule" applicable in every case.¹⁶ Where the cashier is the sole representative of the bank in a transaction, and does not deal with the bank or with any other agent acting for it, the knowledge of the cashier is imputed to the bank notwithstanding he has an opposing personal interest or he is engaged in a personal fraud against the bank.¹⁷

§ 2256. Knowledge as imputed to officer—Notice to one officer or agent as notice to other officers or agents. Where a statute requires notice to directors, notice to the president alone is not sufficient.¹⁸ The fact that a land company owned the land and factory used by a piano company, and that the same persons were stockholders and practically the owners of both corporations, does not impute notice to one elected secretary of the land company of the financial condition of the piano company in which he was not a stockholder.¹⁹

§ 2257. — Knowledge of officer as imputed to himself as individual. The fact that an indorser on a corporate note is also a director, with full knowledge of the corporate affairs, does not excuse the lack of notice of presentment and dishonor.²⁰

XXIV. OFFICERS CONSIDERED AS TRUSTEES OR FIDUCIARIES

A. General Rules

§ 2261. Directors and other officers as trustees or agents—General rule. Directors and other managing officers are often referred to as, or expressly held to be, trustees.²¹ Sometimes

¹⁵ *Western Securities Co. v. Silver King Consol. Min. Co.*, — Utah —, 192 Pac. 664, citing *Fletcher Cyc. Corp.*, § 2251.

¹⁶ *Goldstein v. Union Nat. Bank*, 109 Tex. 555, 213 S. W. 584.

¹⁷ *National Bank v. Whitney*, — Cal. App. —, 180 Pac. 845. To same effect, see *State Bank of Morton v. Adams*, 142 Minn. 63, 170 N. W. 925.

¹⁸ *Conway v. First Nat. Bank*, 256 Fed. 277.

¹⁹ *Ironbound Trust Co. v. Schmidt-Dauber Co.*, 102 N. Y. Misc. 708, 169 N. Y. Supp. 524.

²⁰ *Keiser v. Butte Creek Consol. Dredging Co.*, — Cal. App. —, 191 Pac. 552, following *Hudson Furniture Co. v. Harding*, 70 Fed. 468, 30 L. R. A. 513, and disapproving *Hull v. Myers*, 90 Ga. 674, 16 S. E. 653.

²¹ *Reinhardt v. Owensboro Planing Mill Co.*, 185 Ky. 600, 215 S. W. 523. See *Beach v. Williamson*,

the holding is merely that the relation of the directors to the "stockholders" is essentially that of trustee and cestui que trust.²² It has been said that the relation is more that of a trustee than that of an agent,²³ and, on the other hand, that directors are not trustees in the true sense of the term but are managing agents.²⁴ In any event, directors sustain a fiduciary relation to the stockholders.²⁵

The president of a corporation who misappropriates corporate money, intrusted to him to purchase land, acts in a "fiduciary capacity," within the Bankruptcy Act, so that the claim is not barred by his discharge in bankruptcy.²⁶

§ 2264. — Double character of agent and trustee. In all dealings with third persons, directors are agents of the corporation; but they are trustees in relation to the corporation.²⁷

§ 2270. Relation to individual stockholders. In New York, it is held that there is no trust relation between an officer and the corporation as to the stock but only as to the corporate properties;²⁸ but it is also held in the same state that officers and managing directors of a corporation are in duty bound to disclose to other stockholders sales of stock by them at a price

— Fla. —, 83 So. 860, citing Fletcher Cyc. Corp., §§ 2261-2271.

Duties as trustee, see *Globe Woolen Co. v. Utica Gas & Electric Co.*, 224 N. Y. 483, 121 N. E. 378.

²² *Kavanaugh v. Kavanaugh Knitting Co.*, 226 N. Y. 185, 123 N. E. 148, rev'g on other grounds 184 N. Y. App. Div. 650, 172 N. Y. Supp. 576; *Glenn v. Kittanning Brewing Co.*, 259 Pa. 510, L. R. A. 1918 D 738, Ann. Cas. 1918 D 769, 103 Atl. 340.

Directors are trustees for all the stockholders. *Glenn v. Kittanning Brewing Co.*, 259 Pa. 510, L. R. A. 1918 D 738, Ann. Cas. 1918 D 769, 103 Atl. 340.

The rule in regard to the duty of directors, as trustees for the stockholders, reaches further than

to transactions occurring directly between the directors and the corporation. *Farwell v. Pyle-National Electric Headlight Co.*, 289 Ill. 157, 10 A. L. R. 363, 124 N. E. 449, aff'g 212 Ill. App. 450.

²³ *Bank of Commerce v. Goolsby*, 129 Ark. 416, 196 S. W. 803.

²⁴ *Jones Min. Co. v. Cardiff Mining & Milling Co.*, — Utah —, 191 Pac. 426, citing *Fletcher Cyc. Corp.*, § 2261.

²⁵ *Proctor v. Farrar*, — Mo. —, 213 S. W. 469.

²⁶ *In re Bloemecke*, 265 Fed. 343.

²⁷ *National Drama Corporation v. Burns*, — N. Y. Misc. —, 183 N. Y. Supp. 739.

²⁸ *East Lake Lumber Co. v. Van Gorder*, 105 N. Y. Misc. 704, 174 N. Y. Supp. 38.

in excess of the amount received by the others under the same sales arrangement.²⁹

§ 2271. Relation to creditors. If the corporation is insolvent, the directors are also trustees for the creditors.³⁰

§ 2272. Duties and responsibilities arising from nature of office. The duty of director as trustee is the duty of constant and unqualified fidelity and is not a thing of forms and phrases. He may stand aloof, while others act, if all is equitable and fair. He cannot rid himself of the duty to warn and to denounce if there is improvidence or oppression, either apparent on the surface or lurking beneath the surface, but visible to his practiced eye.³¹

§ 2275. Title to and possession of corporate property. If an officer mingles his funds with those of the corporation, the latter cannot claim the entire fund.³²

§ 2277. Engaging in rival business. Whether an agreement by a retiring officer of a corporation not to go into any like business is in restraint of trade depends on the rules governing such contracts generally.³³

§ 2279. Sale of influence in management of company. An agreement, on selling stock, to cause the purchaser to be elected a director and secretary of the corporation, is illegal, although the seller owned nearly all the stock.³⁴

B. Acquiring Adverse Title or Interests

§ 2281. General rule. Property purchased by corporate officers in their own name, but with corporate funds, is impressed

²⁹ Terry v. Green, 185 N. Y. App. Div. 517, 173 N. Y. Supp. 309.

³⁰ Shoenenthal v. New Jersey Gardens Co., — N. J. Eq. —, 103 Atl. 415.

³¹ Globe Woolen Co. v. Utica Gas & Electric Co., 224 N. Y. 483, 121 N. E. 378.

³² J. Austin Dunn Specialty Co. v. Dunn, 202 Ill. App. 206.

³³ Heinz v. National Bank of Commerce, 237 Fed. 942.

³⁴ Fabre v. O'Donohue, 185 N. Y. App. Div. 779, 173 N. Y. Supp. 472.

with a trust in favor of corporate creditors.³⁵ Conspiracy of the directors and others to themselves acquire the corporate property and wreck the corporation authorizes, it seems, an action to enforce a constructive trust.³⁶

§ 2282. Limitations of and exceptions to rule. Acquisition of property by an officer of a corporation does not inure to the benefit of the corporation unless the corporation had already had an existing interest in such property, or an expectancy growing out of such existing right, or where the acquisition will in some degree prevent or hinder the corporation in effecting the purpose of its creation.³⁷

§ 2283. Illustrations of rules—In general. A corporate officer who buys stocks in his own name with corporate funds is a constructive trustee of the stocks for the company.³⁸ Directors owning a majority of the stock act in fraud of the other stockholders where they buy a license contract which the corporation was financially able to buy, and thereby make large profits which might have inured to the corporation if it had bought.³⁹ Directors are guilty of breach of trust where they allow the company to abandon an option contract to purchase a mining claim, and secretly acquire the claim themselves, accept payments, and then declare a forfeiture for nonpayment, and they cannot justify themselves on the theory that until they got their money back they were entitled to protect themselves by secrecy.⁴⁰ A director and general manager of a mining company may purchase adjoining ore land and lease it to the company, where the company was financially unable to purchase it and he offered the company the benefit of the purchase.⁴¹

§ 2284. — Obtaining assignment of corporate contract from other party thereto. A director has no right to buy an execu-

³⁵ Sparks v. McCraw, 112 S. C. 519, 100 S. E. 161.

³⁶ Munro v. Smith, 259 Fed. 1.

³⁷ Tierney v. United Pocahontas Coal Co., — W. Va. —, 102 S. E. 249, citing Fletcher Cyc. Corp., § 2281.

³⁸ Millard v. Green, — Conn. —, 110 Atl. 177.

³⁹ Farwell v. Pyle-National Elec. Headlight Co., 212 Ill. App. 450.

⁴⁰ Munro v. Smith, 259 Fed. 1, 22, rev'g 243 Fed. 654.

⁴¹ Presidio Min. Co. v. Overton, 261 Fed. 933.

tory corporate contract for his own profit where by so doing his interests become adverse to those of the corporation.⁴²

§ 2285. — Renewal of lease or purchase of leased property. The president of a bank cannot take a lease of the premises occupied by the bank for his own personal interests as opposed to those of the bank.⁴³

D. Purchase at Judicial, Execution or Tax Sale

§ 2292. Always voidable where purchase a breach of trust or not in good faith. A director who purchases corporate property at a foreclosure sale takes no title where he has actual or constructive notice of proceedings which rendered the bonds invalid.⁴⁴

§ 2294. View that purchase not voidable where fair and in good faith. Where stockholders who are also directors purchase corporate property at execution or foreclosure sale, at its fair value and in good faith, the sale will not be set aside where the other stockholders failed to act.⁴⁵

§ 2295. Purchase to protect debt or rights of officer. Directors may take a mortgage to protect a loan by them to the corporation, may foreclose the mortgage, and may purchase at the foreclosure sale.⁴⁶ Where a director is a creditor he may enforce against the corporation a note given to him, at least where notice is given to each of the stockholders personally, and he may purchase at the execution sale.⁴⁷

§ 2296. Rule as affected by insolvency of corporation. The president and sole stockholder of a corporation may purchase its assets at a forced sale, where the creditors of the corporation

⁴² Farwell v. Pyle-National Elec. Headlight Co., 289 Ill. 157, 10 A. L. R. 363, 124 N. E. 449, aff'g 212 Ill. App. 450.

⁴³ Paw Paw Sav. Bank v. Free, 205 Mich. 52, 171 N. W. 464.

⁴⁴ Hess Warming & Ventilating Co. v. Burlington Grain Elevator Co., — Mo. —, 217 S. W. 493.

⁴⁵ Wiley v. Reaser, — W. Va. —, 103 S. E. 362.

⁴⁶ McKee v. Interstate Oil & Gas Co., 77 Okla. 260, 188 Pac. 109.

⁴⁷ Grunden v. German, — Wash. —, 188 Pac. 491.

had assumed full control and the president had nothing to do with procuring the sale.⁴⁸

E. Profits Made by Officer

§ 2303. **General considerations and rules.**⁴⁹ A corporate officer cannot make a profit out of his trust or agency without making disclosure to the corporation.⁵⁰ Thus, directors cannot take advantage of their official position to obtain a personal profit to the detriment of the stockholders.⁵¹ So the president of a corporation cannot use corporate property nor his office for private gain.⁵² A majority of the stockholders at a meeting cannot ratify the retention of secret profits by directors, against the objection of any stockholders.⁵³

§ 2304. **Limitations of rule.** An ex-director of a corporation seeking merger with another corporation, although he had assisted the scheme while a director, is not a trustee for the corporation of stock afterwards acquired by him in the second corporation.⁵⁴ Co-directors owning half the stock of a corporation cannot compel the other directors owning the other half, to account for secret profits from a lease by the corporation which resulted in benefits to the latter, where complainants do not come into equity with clean hands, they having secretly obtained an advantage over the other directors in dealing with the lessee.⁵⁵

⁴⁸ McMullin v. Westinghouse's Estate, 259 Pa. 216, 103 Atl. 57.

⁴⁹ Right of corporation to profits made by officers, see articles in 4 Minn. L. Rev. 513-520.

⁵⁰ Cleveland-Cliffs Iron Co. v. Arctic Iron Co., 261 Fed. 15; Paw Paw Sav. Bank v. Free, 205 Mich. 52, 171 N. W. 464; Keely v. Black, — N. J. L. —, 111 Atl. 22; North American Coal & Coke Co. v. O'Neal, 82 W. Va. 186, 95 S. E. 822; Roxborough Gardens of Hamilton v. Davis, 52 Dom. L. Rep. (Can.) 572; Crawford v. Bathurst Land & Development Co., Ltd., 43 Dom. L. Rep. (Can.) 98.

⁵¹ Axford v. Western Syndicate Inv. Co., 141 Minn. 412, 168 N. W. 97, 170 N. W. 587; Glenn v. Kittanning Brewing Co., 259 Pa. 510, L. R. A. 1918 D 738, Ann. Cas. 1918 D 769, 103 Atl. 340, applying rule to purchase by directors of new issue of stock.

⁵² Keely v. Black, 90 N. J. Eq. 439, 107 Atl. 825.

⁵³ Crawford v. Bathurst Land & Development Co., Ltd., 43 Dom. L. Rep. (Can.) 98.

⁵⁴ Holmes v. Doe Run Lead Co., — Mo. App. —, 223 S. W. 772.

⁵⁵ Cleveland-Cliffs Iron Co. v. Arctic Iron Co., 261 Fed. 15, 22-25.

§ 2307. **Good faith of officer or want of damage to corporation as immaterial.** The fact that a contract is beneficial to the corporation does not absolve the officer from liability for secret profits.⁵⁶

§ 2311. **Bribes or presents from third persons.** Gifts, gratuities or bribes given to a director to influence his official action must be accounted for by him and surrendered to the company.⁵⁷

§ 2312. **Right to patents or inventions.**⁵⁸

§ 2318. **Miscellaneous applications of rule—Sales or leases by or to the corporation.** A director is liable to the corporation for secret profits made in a sale of property by him to the corporation, he having bought it with knowledge that the corporation desired and intended to purchase it.⁵⁹ Where a director knew there was a possibility of selling certain corporate property for eighty thousand dollars, and with such knowledge secured an option on the property from his co-directors, to purchase for fifty thousand dollars, without disclosing the anticipated profits, he cannot retain the profits made.⁶⁰ Where a corporation authorized two of its directors to sell certain land but not "for less than ten thousand dollars" such authority does not entitle such directors to any sum they sell the property for in excess of the ten thousand dollars.⁶¹ The president of a corporation who assumes to act as a salesman in disposing of all its assets cannot secure to himself advantages not common to all the stockholders.⁶² Where a general manager makes secret profits by purchasing material in addition to the amount purchased by him for the corporation, and he could have purchased it all for the corporation, such profits belong to the corporation.⁶³

⁵⁶ Keely v. Black, 90 N. J. Eq. 439, 107 Atl. 825, citing Fletcher Cyc. Corp., § 2307.

⁵⁷ Keystone Guard v. Beaman, 264 Pa. 397, 107 Atl. 835.

⁵⁸ Title to patent as between general manager and corporation, see Dowse v. Federal Rubber Co., 254 Fed. 308.

⁵⁹ Highland Park Inv. Co. v.

List, — Cal. App. —, 184 Pac. 48.

⁶⁰ H. B. Cartwright & Bro. v. United States Bank & Trust Co., 23 N. M. 82, 167 Pac. 436.

⁶¹ Proctor v. Farrar, — Mo. —, 213 S. W. 469.

⁶² Garber v. Town, 208 Mich. 1, 175 N. W. 487, 176 N. W. 960.

⁶³ Michigan Crown Fender Co.

§ 2319. — **Sale of stock.** The president of a corporation is not liable over to the corporation for profits made by him in purchasing and reselling stock of the corporation acquired from stockholders.⁶⁴

§ 2321. — **Giving up office for consideration.** A secret profit realized by a director from an undertaking to deliver the corporate control of his company inures to the corporation.⁶⁵

F. Rights as Creditors of Corporation

§ 2325. **In general.** A director or other officer who, as creditor, pays a claim against the corporation, is entitled to subrogation the same as creditors generally.⁶⁶

§ 2326. **Security for or payment of debt.** A corporation may secure a present loan to it by a director by giving him a mortgage.⁶⁷ Directors may secure their claims against the corporation by taking a judgment against the corporation, where there is no fraud.⁶⁸ The general manager of a corporation owning a ship is not entitled to a maritime lien for services rendered or money advanced.⁶⁹

XXV. PERSONAL DEALINGS OF OFFICER WITH CORPORATION OR WITH CORPORATE PROPERTY

§ 2331. **Effect of statutes and by-laws.** A clause in incorporation papers providing that, in the absence of fraud, no action taken by a majority of the directors shall be invalid because some or all of the directors are interested therein, is against public policy if to be construed as validating a transfer of all the common stock to certain incorporators for an option worth much less than the stock.⁷⁰

v. Welch, 211 Mich. 148, 178 N. W. 684.

⁶⁴ Keely v. Black, — N. J. L. —, 111 Atl. 22.

⁶⁵ Keely v. Black, 90 N. J. Eq. 439, 107 Atl. 825, citing Fletcher Cyc. Corp., § 2321, and see §§ 1753, 1754, supra.

⁶⁶ Geisenberger & Friedler v. Robert York & Co., 262 Fed. 739;

Caldwell v. Robinson, 179 N. C. 518, 103 S. E. 75.

⁶⁷ In re Lake Chelan Land Co., 257 Fed. 497, 5 A. L. R. 557.

⁶⁸ Caldwell v. Robinson, 179 N. C. 518, 103 S. E. 75.

⁶⁹ The Gyda, 235 Fed. 266.

⁷⁰ Whalen v. Hudson Hotel Co., 183 N. Y. App. Div. 316, 170 N. Y. Supp. 855.

§ 2332. General rules without reference to whether interested officer represents corporation or whether corporation represented by other officers—In general. A contract between a corporation and one of its directors, where not fraudulent, is valid.⁷¹ An officer of a corporation can deal with the corporation if his acts are open and fair and known to the directors and stockholders.⁷² Where the grantee of corporate land is its president and substantial owner, he is not a bona fide purchaser so as to prevent a decree of specific performance of a prior contract by the corporation to sell the land to another.⁷³

§ 2333. — Dealings as void or voidable. A contract between a corporation and a director, made by the legal action of the board of directors, is binding until nullified on the ground of fraud.⁷⁴

§ 2334. — Transaction as subject to careful scrutiny by courts. Dealings between an officer of a corporation and his board of directors must be scrutinized carefully to see that the corporation is not injured thereby.⁷⁵

§ 2335. — Necessity that transaction be fair and not a breach of trust. Dealings between a corporation and a director or other officer are voidable unless open, in good faith, fair and fully understood.⁷⁶ Whenever there is a personal and adverse interest in a director, in his dealings with the corporation, there must be the utmost fairness and good faith in guarding the interest of the corporation.⁷⁷ Where a director deals with his corporation, he must make a full and fair disclosure to the other directors of all the circumstances attending the proposed

⁷¹ Congress Hotel Co. v. Southgate, 209 Ill. App. 442.

⁷² Quinn v. Quinn Mfg. Co., 201 Mich. 664, 167 N. W. 898.

⁷³ Morris v. Basnight, 179 N. C. 298, 102 S. E. 389.

⁷⁴ Puller v. Royal Casualty Co., 271 Mo. 369, 196 S. W. 755.

⁷⁵ Garber v. Town, 208 Mich. 1, 175 N. W. 487, 176 N. W. 960.

⁷⁶ Jordan v. Jordan Co., — Conn.

—, 109 Atl. 181; Club Laundry & Cleaning Co. v. Murphy, — Pa. —, 109 Atl. 622.

Contracts of an officer whereby he substitutes himself as a corporate debtor and releases the original debtor cannot be upheld where clearly antagonistic. W. C. Zachow Co. v. Grignon, — Wis. —, 179 N. W. 593.

⁷⁷ Noyes v. Wood, 247 Fed. 72.

transaction and the extent of the benefit which he will receive.⁷⁸

§ 2337. — Presumptions and burden of proof. The burden is on a director to show the fairness of his dealings with the corporation.⁷⁹ While a director may purchase property from the corporation, he has the burden of showing the purchase was in good faith and for a fair price.⁸⁰

§ 2338. Dealings where officers adversely interested represent the corporation—General considerations. An officer cannot represent both himself and the corporation where his personal interests are adverse to those of the corporation.⁸¹

§ 2344. — Effect of ownership of all of stock by contracting directors. A sale to a corporation by its directors of their own property at their own price is not void nor voidable at the instance of the corporation itself if at the time of the transaction the directors were the only stockholders.⁸²

§ 2347. Dealings between director or other officer and the corporation when it is represented by other directors or officers—Majority rule that contract or transaction is valid if fair and in good faith. Where corporations A and B contract with each other, and a common director abandons his functions as director of A and negotiates only on behalf of B, and so notifies his associate directors of A, the contract can be avoided by A only where it is unfair to A.⁸³

§ 2353. Under what circumstances officer may be said to represent corporation—Where majority of directors deal with themselves. A board of directors cannot contract where a majority are adversely interested.⁸⁴

⁷⁸ H. B. Cartwright & Bro. v. United States Bank & Trust Co., 23 N. M. 82, 167 Pac. 436.

⁷⁹ Jordan v. Jordan Co., — Conn. —, 109 Atl. 181; First State Bank v. Lang, — Mont. —, 174 Pac. 597.

⁸⁰ Jordan v. Jordan Co., — Conn. —, 109 Atl. 181.

⁸¹ F. T. Gunther Grocery Co. v. Hazel, 179 Ky. 775, 201 S. W. 336.

⁸² Sargent v. Palace Café Co., 175 Cal. 737, 167 Pac. 146.

⁸³ Cleveland-Cliffs Iron Co. v. Arctic Iron Co., 261 Fed. 15.

⁸⁴ Miley v. Heaney, 168 Wis. 58, 169 N. W. 64.

§ 2354. — **Where presence of interested director necessary to make a quorum.** A mortgage loan by two directors to a corporation is not invalid because the mortgage was authorized at a directors' meeting where only two others of the five directors were present, since the presence of a quorum of disinterested directors was not necessary.⁸⁵

§ 2355. — **Where interested director dominates other directors.** Fraud in the making of a contract between a corporation and one of its directors cannot be based on such director dominating the board where the corporation refused to act and remained passive for fifteen years after the alleged domination had ceased.⁸⁶ Refusal of a director to vote, as a member of the executive committee, on a contract made under the dominating influence of such director who was a director of both parties to the contract, does not nullify as of course his influence exerted without a vote.⁸⁷

§ 2364. **Application of general rules to particular transactions—In general.** The fact that a bank has no power to deal in real estate does not preclude a contract between the bank and one of its officers whereby the latter was to pay the bank a dollar an acre on all land sold by him, in consideration of the use of stamps, stationery, time and space belonging to the bank in connection therewith.⁸⁸

§ 2365. — **Purchase of corporate property by director or other officer.** A director or officer may purchase property from the corporation if all is done in good faith.⁸⁹ But directors cannot hold the corporate property received on agreement to pay the corporate debts, where they secreted information concerning the real value of the property.⁹⁰

⁸⁵ Geisenberger & Friedler v. Robert York & Co., 262 Fed. 739.

⁸⁶ Congress Hotel Co. v. Southgate, 209 Ill. App. 442.

⁸⁷ Globe Woolen Co. v. Utica Gas & Electric Co., 224 N. Y. 483, 121 N. E. 378, aff'd 170 N. Y. App. Div. 940, 154 N. Y. Supp. 1123.

⁸⁸ Farmers' State Bank v. Weiland, 41 S. D. 57, 168 N. W. 717.

⁸⁹ Rhea v. Newton, 262 Fed. 345; Howard v. Tatum, 81 W. Va. 561, 94 S. E. 965.

⁹⁰ Beach v. Williamson, — Fla. —, 83 So. 860.

§ 2366. — Sales by directors or other officers to corporation. A sale of property by a director to a corporation can be sustained only where made in good faith.⁹¹ A director may sell land to his corporation, or exchange it for stock and bonds, where the price is fair, there was no intent to defraud, and there were no existing creditors other than the seller.⁹² Where the president acquires property he may sell it to the corporation at a profit, where not above its real value and where it was not bought with the intent of selling it to the company so as to require disclosure of facts.⁹³ A transaction by which one received eight thousand dollars worth of bonds from the corporation for property which had shortly prior thereto cost him only two hundred dollars, when both at the time of his own purchase and the sale to the company, he was its treasurer and field manager, charged with looking after its affairs of that character, is illegal and fraudulent.⁹⁴ Where brokers who sold property to a corporation were stockholders and managing officers, notice by the brokers of their interest should have been given.⁹⁵

§ 2367. — Leases by or to directors or other officers. A lease by a corporation to an officer, where without consideration, is void as to corporate creditors.⁹⁶

§ 2368. — Loans to corporation.⁹⁷ A solvent corporation may borrow money from its directors.⁹⁸ A loan by a director to a corporation, secured by mortgage, is voidable where not

⁹¹ *Drennen v. Southern States Fire Ins. Co.*, 252 Fed. 776.

⁹² *Caldwell v. Robinson*, 179 N. C. 518, 103 S. E. 75.

⁹³ *Southwestern Portland Cement Co. v. Latta*, — Tex. Civ. App. —, 193 S. W. 1115.

⁹⁴ *Parks v. Hughes*, 145 La. 221, 82 So. 202.

⁹⁵ *Newell-Murdoch Realty Co. v. Wickham*, — Cal. —, 190 Pac. 359.

⁹⁶ *Taylor v. Ellsworth Building Corporation*, — N. Y. Misc. —, 183 N. Y. Supp. 394.

⁹⁷ Money furnished by directors to a bank to meet impairment of capital as loan or donation, see *Andrews v. Cosmopolitan Bank*, 183 N. Y. App. Div. 787, 171 N. Y. Supp. 875, rev'g 101 N. Y. Misc. 672, 167 N. Y. Supp. 935.

⁹⁸ *McKey v. Bruns*, 243 Fed. 370; *Hille v. Evans*, — Colo. —, 187 Pac. 315.

Directors may loan money to the corporation to pay pressing debts. In *re Lake Chelan Land Co.*, 257 Fed. 497, 5 A. L. R. 557.

fair and in good faith, but is not void.⁹⁹ Directors of a bank may loan money to it where its capital is impaired, and it is no defense to an action to recover the loan that the fund is not a valid surplus fund.¹

§ 2373. — Issuance of stock to directors or other officers.

A transfer of stock by the corporation to its president is voidable where obtained by fraud.² An agreement by a corporation to pay an officer a certain sum in stock at its par value gives him an undue advantage requiring him to account, where the actual value of the stock was double its par value.³

§ 2376. Transactions between corporations having one or more common directors or other officers—In general. Common directors, in part, does not preclude dealings between two corporations.⁴ Thus, the mere fact that directors sell corporate property to a new corporation of which they are directors does not make the sale absolutely void although the sellers control both corporations.⁵

“The fact,” said Justice Pitney, “that the same persons were directors and managers of both corporations subjects their dealings inter sese to close scrutiny. That two corporations have a majority or even the whole membership of their boards of directors in common does not necessarily render transactions between them void; but transactions resulting from the agency of officers or directors acting at the same time for both must be deemed presumptively fraudulent, unless expressly authorized or ratified by the stockholders; and certainly, where the circumstances show * * * that the transaction would be of great advantage to one corporation at the expense of the other, especially where, in addition to this, the personal interests of the directors, or any of them, would be enhanced at the expense

⁹⁹ Geisenberger & Friedler v. Robert York & Co., 262 Fed. 739.

¹ Andrews v. Cosmopolitan Bank, 183 N. Y. App. Div. 787, 171 N. Y. Supp. 875, rev'g on other grounds 101 N. Y. Misc. 672, 167 N. Y. Supp. 935.

² Cutting v. Woodward, 255 Fed. 633.

³ Garber v. Town, 208 Mich. 1, 175 N. W. 487, 176 N. W. 960.

⁴ Title Insurance & Trust Co. v. Northwestern Long Distance Tel. Co., 88 Ore. 666, 173 Pac. 251.

⁵ Rossing v. State Bank, 181 Iowa 1013, 165 N. W. 254.

of the stockholders, the transaction is voidable by the stockholders within a reasonable time after discovery of the fraud.”⁶

Where a director in a company owning iron ore land,—the company having decided to lease and not to mine the land,—expressly withdraws from negotiations as to the lease with notice to adverse directors to go ahead and do just as they please, the fact that he was interested in the lessee does not render him accountable to the corporation for profits made by the lessee.⁷ In a New York decision of its Court of Appeals, it is held that it is not enough for the common director to merely withdraw from the dealing but that he owes to the one corporation the affirmative duty to disclose an unfair advantage which he knew or should have known would result and of which it is to be assumed his associates were ignorant.⁸

§ 2377. — Where common officer or officers act for both corporations.⁹

§ 2378. — Where unfair or fraudulent.¹⁰ Where dealings between corporations with common directors are of great advantage to one corporation at the expense of the other, and the personal interests of the directors or any of them are enhanced at the expense of stockholders, the transaction is voidable by the stockholders.¹¹

Where a sale between two corporations having a common director is for an inadequate consideration, especially where he is dominating in influence or in character, the sale is voidable and should be set aside at the instance of the selling corporation.¹² Where a sale is voidable for inadequacy of price,

⁶ *Corsicana Nat. Bank of Corsicana v. Johnson*, 251 U. S. 68, 64 L. Ed. 141.

⁷ *Cleveland-Cliffs Iron Co. v. Arctic Iron Co.*, 261 Fed. 15, 20-22.

⁸ *Globe Woolen Co. v. Utica Gas & Electric Co.*, 224 N. Y. 483, 121 N. E. 378, referred to in *Cleveland-Cliffs Iron Co. v. Arctic Iron Co.*, 261 Fed. 15, 19, as “one of the latest and one of the most extreme applications of the rule that we have seen.”

⁹ The New York case referred to in vol. 4, note 36, was later affirmed on the facts by the court of appeals after a retrial, in 224 N. Y. 483, 112 N. E. 378 (see § 2376, *supra*).

¹⁰ Burden of proof as to fairness. see § 2389, *infra*.

¹¹ *Corsicana Nat. Bank of Corsicana v. Johnson*, 251 U. S. 68, 90, 64 L. Ed. 141.

¹² *Geddes v. Anaconda Copper Min. Co.*, — U. S. —, 65 L. Ed. —, 41 Sup. Ct. Rep. 209, *rev'g on*

because of a common director, it should be set aside absolutely. It is improper to order that the property be offered at public auction and if no bid should be received greater than the sale price the sale should be confirmed.¹³

§ 2379. — Where common directors are a minority and their votes not necessary to creation of contract. Where a director in one corporation was its chief stockholder and its president, and in another corporation was a director and chairman of the executive committee but had no property interest therein, a contract between the two corporations made at his instigation will not be enforced against the latter where unfair to it notwithstanding said director refused to vote as a director of the latter as to making the contract, where he executed a dominating influence on the other directors of the latter company.¹⁴

§ 2380. — Application to rules to mere agents or officers other than directors. Service of a notice to quit may be made by an officer of one corporation on an officer of another corporation although both persons were officers in both companies.¹⁵

§ 2386. — Rights of corporations as dependent on for whom officer is really acting.¹⁶

§ 2388. — Presumptions. Contracts between two corporations with interlocking directorates are presumptively invalid, it is held in Oklahoma.¹⁷

§ 2389. — Burden of proof. Contracts between corporations having one or more common directors, while not prohibited nor prima facie void or fraudulent, are voidable unless shown to be

other grounds 245 Fed. 225, which aff'd 222 Fed. 129.

¹³Geddes v. Anaconda Copper Min. Co., — U. S. —, 65 L. Ed. —, 41 Sup. Ct. Rep. 209, rev'g on this ground 245 Fed. 225, which aff'd 222 Fed. 129.

¹⁴Globe Woolen Co. v. Utica Gas & Electric Co., 224 N. Y. 483, 121 N. E. 378, aff'g 170 N. Y.

App. Div. 540, 154 N. Y. Supp. 1123.

¹⁵F. P. McKay Co. v. Savery House Hotel Co., 184 Iowa 260, 168 N. W. 295.

¹⁶On this question, see New York case as set forth in § 2379 of this supplement.

¹⁷Bentley v. Zelma Oil Co., 76 Okla. 116, 184 Pac. 131.

fair and free from wrong.¹⁸ The "fairness of contracts between corporations having directors in common must be shown by clear and convincing proof, and it must be made to appear that they are absolutely free from fraud." ¹⁹

§ 2394. Ratification or authorization of dealings with interested officer—General rule. A contract between a director and his corporation is not voidable where all the stockholders consent thereto and the property acquired thereby is used for the benefit of the corporation.²⁰

§ 2397. — Ratification by majority of stockholders as binding on minority stockholders. A contract made by directors is not invalid because some of the directors were adversely interested where it was ratified by a majority of the stockholders.²¹

XXVI. GENERAL DUTIES AND LIABILITIES OF OFFICERS CONNECTED WITH MANAGEMENT OF CORPORATION

A. General Considerations

§ 2405. Duties and liabilities stated generally.²² Corporate officers cannot be sued in their individual capacities for a purely corporate matter,²³ and it is held that an officer is not liable to a stockholder for mere nonfeasance.²⁴ Directors are not personally liable for a deposit of money as security by agents although, instead of retaining it as a special account, they put it in the general treasury and used it in the business, since the act was a corporate act.²⁵

¹⁸ *Geddes v. Anaconda Copper Min. Co.*, 245 Fed. 225, aff'g 222 Fed. 129.

¹⁹ *City Trust Co. v. Bankers' Mortgage Loan Co.*, 102 Neb. 532, 167 N. W. 785.

²⁰ *McKee v. Interstate Oil & Gas Co.*, 77 Okla. 260, 188 Pac. 109.

²¹ *Thurmond v. Paragon Colliery Co.*, 82 W. Va. 49, 95 S. E. 816.

²² "Motive as affecting personal liability of directors in voting for

acts not in themselves illegal," see note in 4 A. L. R. 166, annotating *Hammond v. Sully*, 48 App. Cas. (D. C.) 320, 4 A. L. R. 160.

²³ *Navajo-Apache Bank & Trust Co. v. Desmond*, — Ariz. —, 170 Pac. 798, which was an action for an accounting.

²⁴ *Orvis v. Lorraine Co.*, 183 N. Y. App. Div. 1, 170 N. Y. Supp. 264.

²⁵ *Wileox v. Gauntlett*, 200 Mich. 272, 166 N. W. 856.

Liability of directors for misconduct is not a fixed but a contingent liability not provable against a bankrupt director.²⁶

§ 2406. Liability of officers other than directors as compared with that of directors.²⁷ The secretary of a corporation is not personally liable for losses occurring, where he assumes the management on the sickness of the president, where he is guilty of no wrongful or fraudulent conduct.²⁸

§ 2408. Statutory liability as precluding common-law liability.²⁹

§ 2409. Persons liable.³⁰

§ 2413. Consent or ratification as precluding liability. A bank cashier is liable to stockholders for negligence, although his acts were authorized by the directors, where he knew or ought to have known that such acts were unlawful.³¹

§ 2414. Right to sue as precluded by laches or estoppel.³²

§ 2415. Contracts inducing disregard of duties.³³ Any contract of directors affecting their duty as such to the detriment of the corporation is illegal; and this applies to a contract under which, if they voted to reduce the salary of one of the officers, they would incur a liability to purchase his shares.³⁴ Thus, a contract whereby two directors agree to vote for each other is illegal.³⁵ So an agreement, in selling stock, to cause the purchaser to be elected a director and secretary, is illegal, although the seller who made the promise owned nearly all the corporate stock.³⁶

²⁶ *In re Hutchcraft*, 247 Fed. 187.

²⁷ "The same doctrine is approved, and also applied in some degree, to the president of a corporation, in *Fletcher's Cyclopaedia of the Law of Corporations*, § 2406." *Boulicault v. Oriel Glass Co.*, — Mo. —, 223 S. W. 423.

²⁸ *Spivey v. Pugh*, 140 Ark. 296, 215 S. W. 739.

²⁹ See § 2647, *infra*.

³⁰ See § 2618, *infra*.

³¹ *Boyd v. Applewhite*, — Miss. —, 84 So. 16.

³² Stockholders' suits, see § 4072 et seq., *infra*.

³³ See also §§ 1753, 1754, *supra*.

³⁴ *Odell v. Wells*, 183 N. Y. App. Div. 242, 171 N. Y. Supp. 345.

³⁵ *Lothrop v. Goudeau*, 142 La. 342, 76 So. 794.

³⁶ *Fabre v. O'Donohue*, 185 N. Y. App. Div. 779, 173 N. Y. Supp. 472.

§ 2416. **Liabilities as joint or several.**³⁷ The negligence may be that of the board of directors collectively, in which case it is a joint liability, or that of one or more directors individually in which case the liability is individual.³⁸ One director who had no knowledge of bookkeeping may be not guilty of negligence resulting in loss of money by a bookkeeper's embezzlement, while another director who was president, manager and treasurer may be guilty of actionable negligence where the bookkeeper was under his supervision.³⁹

B. Breach of Duty in General

§ 2424. **General illustrations of breach of duty.** Directors are not personally liable for causing the corporation to breach a contract with another corporation, especially where a cause of action against the corporation for the breach is enforceable.⁴⁰ Where directors fail to collect any interest, when part of the directors exercise an option to purchase, they are personally liable for such interest as should have been collected.⁴¹ Where a loss on a building contract between a corporation and one of its directors, whereby the former agreed to build a house for the latter, was due to the interference of the director with the other officers of the corporation in regard to letting subcontracts, the director is liable to the corporation for such loss.⁴² Where it was agreed that an attorney should have a certain sum out of a final payment by the city to a corporation under a construction contract, and the corporation was insolvent, the officers of the corporation who collected the full amount without the knowledge of the attorney and applied it to corporate debts, are personally liable to the attorney as in case of a trust fund.⁴³

§ 2432. **Liability for bad loans or investments.**⁴⁴ Actionable negligence of directors of a bank may consist either in making a

³⁷ See also § 2710, *infra*.

³⁸ Tackett v. Green, 187 Ky. 49, 218 S. W. 468.

³⁹ Boulicault v. Oriel Glass Co., — Mo. —, 223 S. W. 423.

⁴⁰ Lukach v. Blair, 108 N. Y. Misc. 20, 178 N. Y. Supp. 8.

⁴¹ Noyes v. Wood, 247 Fed. 72.

⁴² Reinhardt v. Owensboro Plan-

ing Mill Co., 185 Ky. 600, 215 S. W. 523.

⁴³ Lynch v. Conger, 181 N. Y. App. Div. 221, 168 N. Y. Supp. 855.

⁴⁴ Liability of director to bank corporation for making of excessive loans considered in First Nat. Bank v. Noyes, 257 Fed. 593.

loan, renewing it, or failing to collect it.⁴⁵ A bank cashier is liable for making excessive and unauthorized loans to a director.⁴⁶ Where directors purchase assets from a firm of which two of the members are directors, at face value but which prove to be worthless and were known at the time by the directors to be of doubtful value, they are liable to the corporation for the loss.⁴⁷ Bank officers who loan three-fifths of the capital stock of the bank to a canning company in which they own stock, where the amount loaned is three times the capital of the latter, are negligent so as to be personally liable for loss, where the directors took no security.⁴⁸ A director sued for loss to stockholders from excessive loans made to himself cannot show that he did not act for the bank.⁴⁹

C. Acts Ultra Vires or Illegal or Beyond Authority of Particular Officer

§ 2434. General rules. A director is not liable for ultra vires acts of the corporation unless he voted therefor, participated therein, connived thereat, or negligently omitted to perform his duty.⁵⁰

§ 2435. Illustrations of general rules. Directors are liable for misappropriation of funds where they act ultra vires in purchasing stock of the corporation.⁵¹

§ 2438. Effect of ignorance or mistake—In general. Directors are personally liable for damages to the company resulting

Liability of an advisory board of a loan company for negligence in recommending a loan, see *Prudential Trust Co. v. McQuaid*, 45 Dom. L. Rep. (Can.) 346.

⁴⁵ *Harris v. Waters*, 112 N. Y. Misc. 640, 183 N. Y. Supp. 721. See also *Magale v. Fomby*, 132 Ark. 289, 201 S. W. 278, where bank with capital of \$50,000 loaned \$30,000 to canning company in which the officers of the bank had stock.

Renewal of bank paper by directors of a bank may constitute neg-

ligence as against the bank. *Harris v. Rogers*, 190 N. Y. App. Div. 208, 179 N. Y. Supp. 799.

⁴⁶ *Boyd v. Applewhite*, — Miss. —, 84 So. 16.

⁴⁷ *Noyes v. Wood*, 247 Fed. 72.

⁴⁸ *Magale v. Fomby*, 132 Ark. 289, 201 S. W. 278.

⁴⁹ *Boyd v. Applewhite*, — Miss. —, 84 So. 16.

⁵⁰ *Holmes v. Crane*, 191 N. Y. App. Div. 820, 182 N. Y. Supp. 270.

⁵¹ *Noyes v. Wood*, 247 Fed. 72.

from their acts in excess of their powers, although they act in good faith.⁵² Officers of a corporation are presumed to know the extent of corporate indebtedness so that notice thereof need not be given them as guarantors of corporate debts.⁵³

§ 2441. Effect of consent or ratification. A stockholder cannot have redress in equity against directors, for ultra vires acts, when, with full knowledge of the facts, he has assented, although under protest, to such acts, and has accepted the benefit thereof.⁵⁴

D. Negligence

§ 2442. In general.⁵⁵ All the directors stand in the same degree of negligence in retaining as cashier one shown to be unworthy of trust and in lending money contrary to the statute.⁵⁶ One negligent director cannot sue his co-directors for gross negligence.⁵⁷ Directors' liability for negligence is not barred by a discharge in bankruptcy before action brought.⁵⁸

§ 2443. Negligence as question of fact.⁵⁹ What "a director must do in exercising reasonable care in the performance of his duties is always dependent upon the facts."⁶⁰

§ 2444. Effect of officers receiving no compensation.⁶¹ A higher degree of vigilance is required of a director who is paid

⁵² Sheldon v. Bills, 102 Neb. 93, 166 N. W. 117.

⁵³ McGowan v. Wells' Trustee, 184 Ky. 772, 213 S. W. 573.

⁵⁴ Holmes v. Crane, 191 N. Y. App. Div. 820, 182 N. Y. Supp. 270.

⁵⁵ For note on "Liability of officers and directors of building and loan association for loss due to negligence," see 19 N. C. C. A. 539.

⁵⁶ Roseville Trust Co. v. Mott, — N. J. Eq. —, 107 Atl. 462.

⁵⁷ Boyd v. Applewhite, — Miss. —, 84 So. 16.

⁵⁸ Boyd v. Applewhite, — Miss. —, 84 So. 16.

⁵⁹ Liability for negligence of director of building and loan association in particular case, see Four Corners Building & Loan Ass'n v. Schwarzwaelder, — N. J. L. —, 103 Atl. 240.

⁶⁰ Kavanaugh v. Commonwealth Trust Co., 223 N. Y. 103, 119 N. E. 237.

⁶¹ The quotation from Freeman's note in the American State Reports in volume four, Fletcher Cyc. Corp., this section, is referred to in Boulicault v. Oriel Glass Co., — Mo. —, 223 S. W. 423, as "quoted with approval" in Fletcher Cyc. Corp., § 2444.

to devote his entire time to the business than is required of other directors.⁶²

§ 2446. Negligence as slight, ordinary or gross. The relative degree of negligence of the several directors does not affect their liability.⁶³

§ 2450. What constitutes "ordinary" or "reasonable" care—Care required as that which men of ordinary prudence exercise in regard to their own affairs. Directors are bound to use the "same degree of care and vigilance in the performance of their duties as a reasonably prudent and careful man would use in the conduct of his business."⁶⁴ Directors in financial institutions must use the same diligence that men prompted by self-interest generally exercise in their own affairs.⁶⁵

§ 2451. — Care required as that of ordinarily prudent men under similar circumstances. Directors must exercise the diligence which ordinary prudent and diligent men would exercise under similar circumstances.⁶⁶

§ 2455. Degree or amount of care as dependent upon kind of corporation. The character of the corporation is entitled to some consideration in determining the care required of directors.⁶⁷

§ 2460. Particular acts as negligence—In general.⁶⁸ Directors are negligent in failing to hold meetings as required by

⁶² *Boulicault v. Oriel Glass Co.*, — Mo. —, 223 S. W. 423, quoting at length from *Fletcher Cyc. Corp.*, § 2444.

⁶³ *Roseville Trust Co. v. Mott*, — N. J. Eq. —, 107 Atl. 462.

⁶⁴ *Tri-Bullion Smelting & Development Co. v. Corliss*, 186 N. Y. App. Div. 613, 174 N. Y. Supp. 830; *Besseliew v. Brown*, 177 N. C. 65, 97 S. E. 743.

⁶⁵ *Kavanaugh v. Commonwealth Trust Co.*, 223 N. Y. 103, 119 N. E. 237.

⁶⁶ *Bowerman v. Hamner*, 250 U.

S. 504, 63 L. Ed. 1113, aff'g *McCormick v. King*, 241 Fed. 737; *Boulicault v. Oriel Glass Co.*, — Mo. —, 223 S. W. 423. See also *Fell v. Pitts*, 263 Pa. 314, 106 Atl. 574.

⁶⁷ *Boulicault v. Oriel Glass Co.*, — Mo. —, 223 S. W. 423.

⁶⁸ What constitutes negligence of the examining committee of board of directors of a bank, in examining accounts, see *Roseville Trust Co. v. Mott*, — N. J. Eq. —, 107 Atl. 462.

the by-laws and in failing to obtain from the treasurer a statement at each meeting of the financial condition of the corporation.⁶⁹ It is negligence for directors to place bonds of other companies, received as the price of property and allotted to stockholders, in the hands of the secretary, where the corporation had a treasurer who had given a fidelity bond while the secretary had not, and to fail to make any investigation as to the safety of the bonds during the two years they were in such custody prior to their theft.⁷⁰ Employment of accountants by the directors does not of itself show diligence.⁷¹ Directors of banks are negligent when they fail to heed the warning of the bank commissioner, especially where they are all without banking experience.⁷²

§ 2461. — Failure to attend directors' meetings. Wilfully absenting one's self from directors' meetings for years and never making, nor causing to be made, any examination of the affairs of the bank, is negligence.⁷³

§ 2464. Excuses—In general. It is no excuse for negligence that the alleged negligent officer was receiving no compensation either as president or director nor that the management which he exercised had never been expressly delegated to him.⁷⁴ A director is not excused from liability for negligence because he did not attend the directors' meetings as often as other members.⁷⁵ Directors sued for negligence cannot set up as a defense that the corporation was never legally incorporated.⁷⁶

§ 2467. — Nonresidence. Nonresidence or residence at a distance from the location of the bank is no excuse, in case of bank directors.⁷⁷

⁶⁹ *Tri-Bullion Smelting & Development Co. v. Corliss*, 186 N. Y. App. Div. 613, 174 N. Y. Supp. 830.

⁷⁰ *Chadwick v. Holm*, 31 Idaho 252, 170 Pac. 87.

⁷¹ *Tri-Bullion Smelting & Development Co. v. Corliss*, 186 N. Y. App. Div. 613, 174 N. Y. Supp. 830.

⁷² *Roseville Trust Co. v. Mott*, — N. J. Eq. —, 107 Atl. 462.

⁷³ *Bowerman v. Hamner*, 250 U. S. 504, 63 L. Ed. 1113, aff'g *McCormick v. King*, 241 Fed. 737.

⁷⁴ *Dresser v. Bates*, 250 Fed. 525, 540.

⁷⁵ *Bank of Commerce v. Goolsby*, 129 Ark. 416, 196 S. W. 803.

⁷⁶ *Boyd v. Applewhite*, — Miss. —, 84 So. 16.

⁷⁷ *Bowerman v. Hamner*, 250 U. S. 504, 63 L. Ed. 1113, aff'g *McCormick v. King*, 241 Fed. 737.

§ 2468. — **Ignorance.** Ignorance which is the result of gross inattention to duty is no excuse for a director.⁷⁸ It is sometimes held that directors are bound to take notice of what their records show,⁷⁹ and bank directors cannot plead ignorance of what a reasonable examination of the books and papers of the bank would disclose.⁸⁰ However, it has been held that directors of a bank are not bound, as matter of law, to know the contents of the books of the bank, including the accounts therein;⁸¹ and a presumption of knowledge of the affairs of a bank by directors will not be indulged in in favor of another director who is president of the bank.⁸²

§ 2469. — **Want of experience or skill.**⁸³

§ 2471. **Liability of directors of national banks for negligence.**⁸⁴

E. Liability of Directors or Other Officers for Acts of Co-Director or Other Officer

§ 2477. **Liability as dependent upon lack of supervision—In general.** Directors cannot delegate the duty of reasonable supervision,⁸⁵ especially in case of bank directors.⁸⁶ The con-

⁷⁸ *Bowerman v. Hamner*, 250 U. S. 504, 63 L. Ed. 1113, aff'g *McCormick v. King*, 241 Fed. 737.

⁷⁹ *Hartley v. Ault Woodenware Co.*, 82 W. Va. 780, 97 S. E. 137.

A corporation or its receiver cannot base a right of recovery against a third person on ignorance of its directors as to what clearly appears in the books of the corporation. *Porter v. Hallet & Carey Co.*, 40 S. D. 136, 166 N. W. 525, where the receiver of an elevator company sued to recover losses by the manager in speculations on the Chicago Board of Trade.

⁸⁰ *Boyd v. Applewhite*, — Miss. —, 84 So. 16.

⁸¹ *Murray v. Third Nat. Bank*, 234 Fed. 481.

⁸² *First State Bank v. Lang*, 55 Mont. 146, 9 A. L. R. 1139, 174 Pac. 597.

⁸³ Youth and inexperience of director considered as excuse in *Roseville Trust Co. v. Mott*, — N. J. Eq. —, 107 Atl. 462.

⁸⁴ Liability of directors of national bank for defalcations of bookkeeper, for failure to examine books of bank, see *Dresser v. Bates*, 250 Fed. 525.

Statutory liability, see § 2647, *infra*.

⁸⁵ *Woodward v. Stewart*, 149 Ga. 620, 101 S. E. 749.

⁸⁶ *Woodward v. Stewart*, 149 Ga. 620, 101 S. E. 749, where complaint held insufficient.

Directors of a bank, although

tention that directors are shielded from liability because of want of knowledge of wrongdoing on the part of their officers, unless their ignorance of such wrongdoing is the result of gross inattention, is disapproved. Directors must use ordinary diligence.⁸⁷ Directors who fail to examine the corporate books for years or to investigate how the business is being conducted by the manager must be deemed to have constructive knowledge that the manager was speculating in the name of the corporation on the Chicago Board of Trade, as shown by entries in such books.⁸⁸ It is no bar to an action against directors for negligence, resulting in embezzlement by the secretary and general manager, that the directors accepted from the defaulter a part of the money embezzled, in settlement of the default.⁸⁹

§ 2478. Acts of directors in turning over or leaving entire business to others. Where directors turn over the entire management of the business to a particular officer without supervision or control, do not attend directors' meetings, require no bond or reports from such officer, fail to have his accounts audited, etc., they are guilty of negligence making them liable for embezzlements by such officer.⁹⁰

§ 2480. What constitutes negligence—In general.⁹¹ The act of a managing director in signing blank checks payable to the

they may delegate to certain officers the active management of the bank, must exercise a reasonable supervision over such officers. *Woodward v. Stewart*, 149 Ga. 620, 101 S. E. 749.

That bank examiners failed to discover defalcations by a book-keeper tends to show that directors are not liable for failure to properly examine the books of the bank. *Dresser v. Bates*, 250 Fed. 525, modified 251 U. S. 524, 64 L. Ed. 388.

Directors of a bank were held not liable for failure to inspect the depositor's ledger, or call in the pass books and compare them with it, in a particular case, where

they accepted the cashier's statement of liabilities. *Bates v. Dresser*, 251 U. S. 524, 64 L. Ed. 388, modifying 250 Fed. 525.

⁸⁷ *Bank of Commerce v. Goolsby*, 129 Ark. 416, 196 S. W. 803.

⁸⁸ *F. M. Davies & Co. v. Porter*, 248 Fed. 397.

⁸⁹ *Besseliew v. Brown*, 177 N. C. 65, 97 S. E. 743.

⁹⁰ *Besseliew v. Brown*, 177 N. C. 65, 97 S. E. 743, and see § 2477, *supra*.

⁹¹ What constitutes negligence of director in management of bank, see *First Nat. Bank v. Noyes*, 257 Fed. 593.

Liability of directors for losses from acts of cashier, see *Roseville*

company's bookkeeper and never comparing the checks returned with the check book stubs, for a period of years, is negligence, making him liable for embezzlement by the bookkeeper.⁹² Where the president and directors, having entire confidence in the treasurer, furnish him with a quantity of checks countersigned in blank, and permit him to fill them out and use them as the business of the corporation requires, they are guilty of gross negligence rendering them liable for loss resulting therefrom.⁹³ If defalcations of the treasurer could have been detected and prevented by the exercise of ordinary care on the part of the directors, they are personally liable for loss sustained by reason of their negligence.⁹⁴

A director of a bank may be liable not only for improvident loans made by him but also for those made by other officers of the bank of which he has knowledge;⁹⁵ and such a director is liable for bad loans made by the cashier where he paid no attention thereto.⁹⁶

The directors are guilty of a breach of trust where they retain in a responsible position a man who has shown himself to be dishonest and unworthy of trust.⁹⁷

§ 2484. Matters putting directors upon inquiry.⁹⁸

§ 2502. Liability of officers not directors for acts of other officers—President. Even though other directors of a national bank are deemed not guilty of negligence, the president who practically managed it is guilty so as to be personally liable for defalcations by a bookkeeper, where he was warned that the \$12

Trust Co. v. Mott, — N. J. Eq. —, 107 Atl. 462.

Liability of directors' examining committee of trust company for negligence, see Roseville Trust Co. v. Mott, — N. J. Eq. —, 107 Atl. 462.

"Liability of directors for defalcations by executive officer or employee," see note in 2 A. L. R. 867-879.

⁹² Boulicault v. Oriel Glass Co., — Mo. —, 223 S. W. 423.

⁹³ Tri-Bullion Smelting & De-

velopment Co. v. Corliss, 186 N. Y. App. Div. 613, 174 N. Y. Supp. 830.

⁹⁴ Tri-Bullion Smelting & Development Co. v. Corliss, 186 N. Y. App. Div. 613, 174 N. Y. Supp. 830.

⁹⁵ Harris v. Cheetham, — N. Y. Misc. —, 180 N. Y. Supp. 106.

⁹⁶ Bank of Commerce v. Goolsby, 129 Ark. 416, 196 S. W. 803.

⁹⁷ Roseville Trust Co. v. Mott, — N. J. Eq. —, 107 Atl. 462.

⁹⁸ See § 2502, *infra*.

a week bookkeeper was leading a fast life and should be watched, but made no investigation although there were other suspicious circumstances.⁹⁹

F. Fraud

§ 2504. General rule.¹ Directors who sell corporate property for a sum much larger than the sum reported to the corporation as the purchase price are liable to minority stockholders for the difference.² Corporate officers are personally liable for a fraudulent issue of stock or stock issued in violation of law.³ The president of a corporation is not individually liable for the fraud of a salesman who was not acting as his agent but as the agent of the corporation.⁴

G. Misappropriation, Conversion or Diversion of Corporate Assets

§ 2505. General rules. Directors are liable to the corporation for wrongfully dealing with or appropriating corporate assets,⁵ and the burden is on them to show application of the proceeds to corporate debts.⁶ If directors waste the corporate property, or apply it in payment of claims which they have no authority to pay, or by negligent inattention to their duties suffer others to appropriate it without right, they are liable to the corporation for any losses resulting from such misuse of authority or neglect of duty.⁷ So a corporation may sue its president for money wrongfully withheld.⁸

⁹⁹ *Bates v. Dresser*, 251 U. S. 524, 64 L. Ed. 388, aff'g 250 Fed. 525.

¹ Liability of directors for fraud, see *Hough v. Commercial Wheat Growers Co.*, 212 Ill. App. 306.

Liability of nonresident directors of corporations for losses by resident's frauds, see article in 12 Illinois L. Rev. 356-364.

² *Proctor v. Farrar*, — Mo. —, 213 S. W. 469.

³ *Fish v. White*, — Iowa —, 175 N. W. 748.

⁴ *Arnold v. Somers*, 92 Vt. 512, 105 Atl. 260.

⁵ *Jones Min. Co. v. Cardiff Mining & Milling Co.*, — Utah —, 191 Pac. 426.

⁶ *Zaring v. Kelly*, — Ind. App. —, 128 N. E. 657.

⁷ *Lake Harriet State Bank v. Venie*, 138 Minn. 339, 165 N. W. 225.

⁸ *Club Laundry & Cleaning Co. v. Murphy*, — Pa. —, 109 Atl. 622.

§ 2509. **Illustrations of rules—In general.** Payment of interest by directors, where not provided for in the contract, is an illegal diversion of funds for which the participating directors are liable.⁹ Directors are not guilty of wastefulness because they spend money to resist a receivership.¹⁰

§ 2511. — **Stock transactions.** Where stock is sold and the proceeds fraudulently appropriated with the approval and connivance of the directors of the company, they are liable to the corporation for the amount of the sale.¹¹

§ 2512. — **Payment of personal debts of officers.** A corporate officer converts corporate property by turning it over in payment of his individual debt.¹²

§ 2515. **Payment of debts.** A treasurer is not guilty of misappropriation of funds where he pays them out on the order of the proper officer.¹³

XXVII. LIABILITY OF OFFICERS ON CORPORATE CONTRACTS OR FOR DEBTS OF THE CORPORATION

§ 2520. **Authorized contract for disclosed principal.** Directors not parties to a corporate contract are not liable thereon.¹⁴ The president is not liable on a contract made by him for the corporation within the scope of his authority, where he acted in a representative capacity for a disclosed principal.¹⁵ The president of a religious society is not liable personally for a broker's commission, where he acted solely for the church, to the knowledge of the broker.¹⁶ The secretary of a corporation ordinarily is not personally liable on corporate contracts.¹⁷ A person act-

⁹ Noyes v. Wood, 247 Fed. 72.

¹⁰ Godley v. Crandall & Godley Co., 181 N. Y. App. Div. 75, 168 N. Y. Supp. 251.

¹¹ James v. P. B. Steifer Min. Co., 35 Cal. App. 778, 171 Pac. 117.

¹² Bronaugh v. Evans, — Ala. —, 85 So. 556.

¹³ Hubert v. American Surety Co., — N. M. —, 192 Pac. 487.

¹⁴ Lukach v. Blair, 108 N. Y. Misc. 20, 178 N. Y. Supp. 8.

¹⁵ Dodson Coal Co. v. Delano, — Pa. —, 109 Atl. 676.

¹⁶ Winokur v. Federman, — N. Y. Misc. —, 183 N. Y. Supp. 41.

¹⁷ Condit v. Merritt Printing & Stationery Co., — Colo. —, 184 Pac. 381.

ing as agent of a company of which he was president is not personally liable for money had and received unless he actually received the money.¹⁸ However, officers of a corporation who buy goods under an agreement to turn over to the seller the proceeds of all cash sales and notes received for sales are personally liable to the seller where they do not turn over such proceeds as agreed on but instead treat them as ordinary receipts.¹⁹

Mere failure to file the new corporate name, where the change has been duly authorized by the stockholders, does not make corporate officers personally liable on a corporate contract where the corporation itself was liable so that the other party to the contract was not injured.²⁰

The rule as to interference with a contract right, as a tort, should not, it seems, be extended so as to make directors liable for breach of a corporate contract, especially where an enforceable judgment could be obtained against the corporation itself for such breach of contract.²¹

§ 2521. Personal liability expressly agreed upon. A corporate officer is not liable personally on his contract where based on no consideration.²²

§ 2522. Personal liability as undisclosed agent for corporation. Conversely, parol evidence may be invoked to hold a corporation on a contract entered into by its president or manager in his own name, if it was intended for and inured to the benefit of the corporation, and there is anything on the face of the instrument suggesting that it was made for an undisclosed principal.²³

§ 2523. Liability in case of pretended but nonexisting corporation. The president of a corporation is not personally liable

¹⁸ Waiters' Benevolent Ass'n v. Cella, — Mo. App. —, 223 S. W. 444.

¹⁹ Peruvian Guano Corporation v. Thompson, — S. C. —, 99 S. E. 808.

²⁰ Pilsen Brewing Co. v. Wallace, 291 Ill. 59, 8 A. L. R. 579, 125 N. E. 714.

²¹ Lukach v. Blair, 108 N. Y. Misc. 20, 178 N. Y. Supp. 8.

²² Crohon & Roden Co. v. Rudnick, 232 Mass. 555, 122 N. E. 741.

²³ Swartz v. Burr, — Cal. App. —, 185 Pac. 411, and see §§ 1491, 1492, supra.

on a contract executed by the secretary, with the president's knowledge, on behalf of the corporation in its new name under the mistaken belief that such new name had been legally acquired.²⁴

§ 2525. Personal liability where officer exceeds his authority—**General rule.** A corporate officer who acts beyond his authority is personally liable on the contract.²⁵

XXVIII. LIABILITY OF OFFICERS TO THIRD PERSONS FOR TORTS

§ 2535. Statement of general rule. An officer who commits a tort as such officer is nevertheless personally liable therefor,²⁶ and a director or managing officer is personally liable for torts which he commands to be done.²⁷ The immunity of charitable corporations from liability for torts does not extend to its officers.²⁸

Ratification of fraudulent acts of corporate officers does not affect the personal liability of such officers.²⁹

§ 2536. Participation in tort as essential to liability. A corporate officer is not liable for the torts of others as employees of the company unless actually a participant or directing the acts.³⁰ For instance, the general manager of a corporation who owns nearly all its stock is not liable for a tort of the corporation unless the injury resulted from his mismanagement, misconduct or negligence.³¹ But where a corporation is a mere shell used by the managing officer to escape liability for unfair com-

²⁴ *Pilsen Brewing Co. v. Wallace*, 214 Ill. App. 540.

²⁵ *Mueller v. Nugent*, 187 Ky. 61, 218 S. W. 730.

The president is personally liable on a contract entered into by him beyond his authority. *Clinchfield Fuel Co. v. Henderson Iron Works Co.*, 254 Fed. 411.

²⁶ *Hitchcock v. American Plate Glass Co.*, 259 Fed. 948, 953; *Gloster Lumber Co. v. Wilkinson*, 118 Miss. 289, 79 So. 96.

²⁷ *Hitchcock v. American Plate Glass Co.*, 259 Fed. 948.

²⁸ *O'Neill v. Odd Fellows Home*, 89 Ore. 382, 174 Pac. 148.

²⁹ *Wright v. Barnard*, 248 Fed. 756.

³⁰ *Beauchamp v. Winnsboro Granite Corporation*, — S. C. —, 101 S. E. 856.

³¹ *Sterns Lumber Co. v. John H. Rice Co.*, 260 Fed. 434.

petition, he is personally liable for the damages from such unfair competition.³²

§ 2540. Conversion—Funds held in trust by the corporation. A corporate officer may be liable for conversion for withholding trust property.³³

§ 2542. Fraud or deceit—In general.³⁴ A corporate officer is not liable for fraud unless damages have resulted,³⁵ but liability is not affected by whether he derived a profit from the fraud.³⁶

§ 2544. Fraudulent representations as to financial condition of company—In general. Officers of corporations are personally liable for false representations as to the financial condition of the corporation.³⁷ Thus, directors are personally liable to one who extends credit to the corporation, when insolvent, in reliance on false financial statements given to mercantile agencies by the directors.³⁸ Misrepresentations of the president of a company that money had been arranged for to meet payments, to induce a contractor to erect a building for the corporation, make the officer personally liable.³⁹

Representations of the value of stock sold by corporate officers, where false, are actionable on the part of the buyer where the officers had superior knowledge as to facts affecting the value, and where an investigation would be required to discover the truth.⁴⁰

³² *Prest-O-Lite Co. v. Acetylene Welding Co.*, 259 Fed. 940. See also § 22 et seq., supra.

³³ *Crohon & Roden Co. v. Rudnick*, 232 Mass. 555, 122 N. E. 741.

³⁴ *Elements of liability of directors for fraud in inducing a subscription to stock*, see *Reno v. Bull*, 226 N. Y. 546, 124 N. E. 144, rev'g 179 N. Y. App. Div. 891, 165 N. Y. Supp. 1109.

³⁵ *Mahon v. Equitable Trust Co.*, 181 N. Y. App. Div. 335, 168 N. Y. Supp. 757.

³⁶ *Munro v. Smith*, 259 Fed. 1, 22.

³⁷ *Alder v. Crozier*, 50 Utah 437, 168 Pac. 83.

³⁸ *Durham v. Wichita Mill & Elevator Co.*, — Tex. Civ. App. —, 202 S. W. 138.

³⁹ *Berlin Const. Co. v. Hoops*, 185 N. Y. App. Div. 277, 173 N. Y. Supp. 117.

⁴⁰ *Redfield v. Lamb*, 103 Neb. 410, 172 N. W. 48, and see § 2564, *infra*.

§ 2547. — **Liability as dependent on participation of officer sought to be held liable.** A “director or other officer of a corporation who approves a report respecting the value of corporate stock which contains untrue and misleading statements of material facts, which report is used, with his knowledge, to induce another to purchase stock in such corporation may become personally liable to a purchaser who in reliance thereon is defrauded thereby.”⁴¹

§ 2553. — **Measure of damages.** The measure of damages for fraud in inducing the sale of stock is the difference between what the seller received for the stock and what he would have received therefor as a participant in the distribution of the sale of the corporate assets, had he retained his stock.⁴²

§ 2555. **Infringement.** Directors are liable personally for infringement of patents where they directed the business⁴³ or where committed by subordinates at their direction.⁴⁴ But a corporate officer is not personally liable for infringement of a patent unless he inflicted the damages or received the profits otherwise than through the usual relations between officer and corporation.⁴⁵ The fact that the only acts of persons infringing a patent were performed by them as officers or directors of a corporation does not necessarily relieve them from liability as infringers.⁴⁶ When “a corporation infringes in obedience to the command of an officer with power to cause the corporation to commit or refrain from committing the infringing act, and when that officer participates in and contributes to the infringement,” he is personally liable as a joint tortfeasor for the infringement.⁴⁷ If a corporate officer is an active participant in infringing a patent, he is liable for costs of the defense which he actively directed.⁴⁸

⁴¹ Redfield v. Lamb, 103 Neb. 410, 172 N. W. 48.

⁴² Staker v. Reese, 82 W. Va. 764, 97 S. E. 641.

⁴³ Eddy v. Kramer, 247 Fed. 962.

⁴⁴ Eddy v. Kramer, 247 Fed. 962.

⁴⁵ D'Arcy Spring Co. v. Marshall Ventilated Mattress Co., 259 Fed. 236.

⁴⁶ Stromberg Motor Devices Co. v. Holley Bros. Co., 260 Fed. 220.

⁴⁷ Hitchcock v. American Plate Glass Co., 259 Fed. 948.

⁴⁸ D'Arcy Spring Co. v. Marshall Ventilated Mattress Co., 259 Fed. 236.

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Where its manager, who was also a majority stockholder, caused a corporation to commit an infringement of a patent, and he indirectly received a part of the infringing profits, the fact that the profits first went to the corporation does not relieve him from liability for the portion thereof which the corporation turned over to him.⁴⁹

§ 2558. Negligence. The president-manager of a corporation is personally liable to an injured boy servant who he put to work in a dangerous place, where, it seems, he would have been liable had he been the owner of the plant.⁵⁰ The president of a corporation who loans his automobile to an employee to use for his own purposes is not liable for injuries while the car was being driven by such employee.⁵¹ It is not negligence for the vice president of a company to sign a deed without reading it, in reliance on a statement of the general attorney of the company that it was a deed for certain property which the directors had voted to convey.⁵²

XXIX. TRANSACTIONS WITH, AND LIABILITIES OF OFFICERS TO, STOCKHOLDERS

§ 2564. Purchase of stock by officer from stockholder—In general.⁵³ An officer of a corporation who purchases its stock is bound to disclose to the seller facts known to him bearing on its value.⁵⁴ An officer of a corporation who buys stock from a stockholder is liable for the difference between the amount paid and its value at the time, where he assures the stockholder

⁴⁹ *Hitchcock v. American Plate Glass Co.*, 259 Fed. 948, 955.

⁵⁰ *Lewis v. Boutilier*, 52 Dom. L. Rep. (Can.) 383.

⁵¹ *Marullo v. St. Pasteur*, 144 La. 926, 81 So. 403.

⁵² *Bailes v. Advance-Rumley Thresher Co.*, 263 Fed. 676.

⁵³ Fraud of director in selling his stock, consisting of false representations, see *Barber v. Keeling*, — Tex. Civ. App. —, 204 S. W. 139.

Duty of a director purchasing

shares of stock, see article in 27 Yale L. J. 731-740.

Note on "Purchase of stock by director as affected by fiduciary relation to stockholders," see Ann. Cas. 1918 B 241, annotating *Dawson v. National Life Ins. Co.*, 176 Iowa 362, L. R. A. 1916 E 878, Ann. Cas. 1918 B 230, 157 N. W. 929.

⁵⁴ *Bettendorf v. Bettendorf*, — Iowa —, 179 N. W. 444, and see § 2544, *supra*.

the price paid is a fair one when he knows of a contract making the stock worth double the amount paid.⁵⁵ Representations of value of stock, where made by a director and treasurer of a corporation supposed to have inside information, are not mere matters of opinion but are actionable where false.⁵⁶ But fraud in acts of corporate officers in purchasing stock at much less than its real value is not shown where the seller knew the facts.⁵⁷

If the officer managing the corporation, by fraud, obtains the stock of a woman of limited business experience, a constructive trust arises and the stock may be followed into the hands of one not a bona fide purchaser.⁵⁸

§ 2565. — Purchase from co-director. A director who has exclusive knowledge of facts affecting the value of the stock is liable in damages to a co-director from whom he purchases his stock where guilty of false representations as to the condition of the company's affairs which induced a sale for less than the value of the stock.⁵⁹

§ 2567. — Rule as affected by special circumstances. A mere nominal director, in purchasing stock, may rely on statements of the president who was salesman and financial agent of the concern, as to the solvency of the corporation and the value of the stock.⁶⁰ A stockholder dealing through a director as his agent, in selling his stock to the president of the company, cannot complain that the latter failed to disclose the financial condition of the company and bought the stock at much less than its real value.⁶¹

⁵⁵ *Bollstrom v. Duplex Power Car Co.*, 208 Mich. 15, 175 N. W. 492.

⁵⁶ *Palmer v. Bratager*, — S. D. —, 172 N. W. 507.

⁵⁷ *Candler v. Heigho*, 208 Mich. 115, 175 N. W. 141.

⁵⁸ *Nesbitt v. Onaway-Alpena Tel. Co.*, 202 Mich. 567, 168 N. W. 519.

⁵⁹ Damages may be recovered by a director who sells his stock to a

co-director through fraudulent representations that a sale of the corporate assets was not contemplated, the latter being the managing head of the company. *Staker v. Reese*, 82 W. Va. 764, 97 S. E. 641.

⁶⁰ *Robinson v. Aldredge*, — Tex. Civ. App. —, 198 S. W. 413.

⁶¹ *Birks v. McNeill*, 185 Iowa 1123, 170 N. W. 485.

Ch. 42] DIRECTORS, OTHER OFFICERS AND AGENTS [§ 2600

XXX. LIABILITY OF OFFICERS TO CREDITORS OF CORPORATION INDEPENDENTLY OF STATUTE

§ 2573. **Wrongful act or omission as essential to liability.** Of course the mere fact that a person is president of a corporation does not make him personally liable for its debts.⁶²

§ 2574. **Liability for nonfeasance or negligence, i.e., mismanagement.** Directors are liable to creditors for losses resulting from their negligent acts, "but the rule as to such liability is largely relative."⁶³

§ 2589. **Right of subsequent creditors to complain.**⁶⁴ Subsequent creditors cannot attack payments by a corporation to its officers as unauthorized.⁶⁵

§ 2590. **Defenses.** Filing of claims of creditors with the receiver does not preclude an action by such creditors against corporate officers pending the receivership.⁶⁶

XXXI. STATUTORY LIABILITY

A. Preliminary Matters

§ 2597. **Statutes as penal or contractual or remedial—General considerations.**⁶⁷ Statutes imposing personal liability on officers for debts consented to by them in excess of the debt limit are not penal but contractual.⁶⁸

§ 2600. — **Statutes as both penal and remedial.** The statutes often are both penal and remedial.⁶⁹

⁶² *Nalty v. Cohn*, 117 Miss. 190, 78 So. 3.

⁶³ *McCullum v. Dollar*, — Tex. —, 213 S. W. 259.

⁶⁴ Subsequent creditors as prejudiced by diversion of corporate funds, see *McCullam v. Buckingham Hotel Co.*, 198 Mo. App. 107, 199 S. W. 417.

⁶⁵ *In re Franklin Brewing Co.*, 263 Fed. 512.

⁶⁶ *Parsons v. Rinard Grain Co.*, 186 Iowa 1017, 173 N. W. 276.

⁶⁷ Whether statutes are penal, see generally *Baker v. Smith*, 41 R. I. 17, 102 Atl. 721.

⁶⁸ *Parsons v. Rinard Grain Co.*, 186 Iowa 1017, 173 N. W. 276.

⁶⁹ *United States Smelting Co. v. Hofkin*, 245 Fed. 896.

§ 2618. Persons liable.⁷⁰ A director elected but who is not notified of his election and does not participate as a director is not liable.⁷¹ A director, although elected "to hold office until the annual meeting to be held on the first Tuesday in April, 1899," is liable for violations of statute after such time where no annual meeting was thereafter held nor new directors elected, and where the by-laws provided that directors shall hold office for one year "or until their successors are duly elected," and where he never resigned but continued to receive a salary.⁷²

B. Particular Statutes

§ 2620. Violation of corporation statutes generally as express ground for personal liability. Failure of directors to collect subscriptions to stock, resulting in insolvency, makes the directors personally liable, under the Indiana statute making directors liable for debts contracted after violation of any of the provisions of the statute which make the company insolvent.⁷³ Statutory liability of directors for wages of servants for at least one year does not cover the claim of a motion picture actress engaged to play parts, she not being a "servant."⁷⁴

§ 2624. Violations of statute as to the incorporation of the company and as to subscriptions to stock—Irregularities and noncompliance with statute in creation or organization of corporation. Officers of a corporation acting as such after an unauthorized change in the corporate name are not personally liable for corporate debts under the statute making officers liable where they assume to exercise corporate powers without complying with the provisions of the statute relating to subscriptions to stock, etc.⁷⁵

⁷⁰ Note on "Statutory liability of officer for debts of corporation as affected by change of officers," see Ann. Cas. 1918 D 796.

⁷¹ Bank of Commerce v. Goolsby, 129 Ark. 416, 196 S. W. 803.

⁷² Baker v. Smith, 41 R. I. 17, 102 Atl. 721.

⁷³ Baltes v. Armour Leather Co., — Ind. App. —, 123 N. E. 356.

⁷⁴ Ryan v. Wills, 44 Dom. L. Rep. (Can.) 634.

⁷⁵ Pilsen Brewing Co. v. Wallace, 291 Ill. 59, 8 A. L. R. 579, 125 N. E. 714.

"Personal liability of officers or stockholders for debts of corporation which has made an unauthorized change in its name," see note in 8 A. L. R. 583, annotating Pilsen Brewing Co. v. Wallace, 291 Ill. 59, 8 A. L. R. 579, 125 N. E. 714.

Section 18 of the Illinois Cor-

§ 2627. — Making and filing certificates of payments of capital stock. A statute making officers and directors liable for failure to make and file a certificate of payment of the capital stock after payment of the last instalment of the stock fixed by the “charter” or by vote of the corporation “in pursuance of the charter or of law” is not confined to corporations created by special statutes, since the word “charter” applies both to the charter of corporations created by special act and to charters of corporations created under general laws.⁷⁶

§ 2630. Incurring debts in excess of debt limit—In general. Statutes often make directors personally liable for permitting the corporate indebtedness to exceed the debt limit.⁷⁷ The Montana statute making directors liable individually where debts are incurred in excess of the capital stock, “in the event of its [the corporation’s] dissolution” is not strictly penal but applies to a practical and not necessarily a judicially adjudged dissolution; and hence it applies where a corporation became insolvent, had no assets, and had ceased to do business, although not judicially dissolved.⁷⁸ The statutory liability of corporate officers for incurring debts in excess of the debt limit is, in Illinois, that of a surety, and the officer assenting thereto cannot compel the other stockholders to contribute.⁷⁹

§ 2632. — What constitutes “assenting to creation” of debts. Mere recognition by a corporate officer of a corporate

poration Act as to liability of corporate officers where corporate powers are assumed without complying with the provisions of the act and before all the stock is subscribed, does not make the president personally liable where the secretary made a contract with his knowledge under a new corporate name not legally acquired. *Pilsen Brewing Co. v. Wallace*, 214 Ill. App. 540.

Under the Illinois statute, any person pretending to be an officer who assumes to exercise corporate powers before compliance with the statutes and before all the stock

is subscribed in good faith, is personally liable for debts incurred by him in the name of the corporation. *Steine & Maley Co. v. Chamales*, 205 Ill. App. 275, applying statute where charter issued but not filed until after contract in question.

⁷⁶ *Baker v. Smith*, 41 R. I. 17, 102 Atl. 721.

⁷⁷ See *Baker v. Smith*, 41 R. I. 17, 102 Atl. 721.

⁷⁸ *Boomer v. Rowe*, 249 Fed. 946, rev’g on this point 244 Fed. 307.

⁷⁹ *Illinois State Bank v. Queen City Quarry Co.*, 203 Ill. App. 176.

debt in excess of the capital stock, or the fact that he might have interposed to prevent such excess, does not make him liable as "assenting" to such indebtedness.⁸⁰ The Iowa statute makes directors and officers "knowingly consenting" to debts in excess of the debt limit, personally liable for such excess. "Knowingly" means with knowledge that the debts exceed the amount permitted by law, i.e., two-thirds of the capital stock. Such want of knowledge cannot be inferred from mere inattention or neglect on the part of the officers sought to be charged. Actual knowledge is required but direct evidence of knowledge is not required.⁸¹

§ 2643. False certificate, notice or report.⁸²

§ 2647. Statutes relating to banks and bank officers—Statutory liability of officers of national banks. Intentional violation is necessary where a director is proceeded against for violating the National Bank Act.⁸³ There is "in effect" an "intentional" violation of the federal statutes whenever a director of a national bank deliberately refuses to examine that which it is his duty to examine.⁸⁴

Common-law liability of directors of national banks for negligence is not affected by the federal statute defining the liability of bank directors.⁸⁵ While the National Bank Statute furnishes the exclusive rule for determining whether its provisions have been violated, so as to hold directors personally liable, it does not prevent the application of the common-law rule for measuring violations of common-law duties.⁸⁶

In an action by a national bank against a director to recover damages for violation of the federal statute forbidding loans to any one person in excess of one-tenth of the capital, liabilities incurred by one person avowedly and in fact as surety or

⁸⁰ Illinois State Bank v. Queen City Quarry Co., 203 Ill. App. 176.

⁸¹ Parsons v. Rinard Grain Co., 186 Iowa 1017, 173 N. W. 276.

⁸² Cause of action as surviving death of officer, see § 2706, *infra*.

⁸³ First Nat. Bank v. Noyes, 257 Fed. 593; Grandprey v. Bennett, — S. D. —, 172 N. W. 514.

⁸⁴ Grandprey v. Bennett, — S. D. —, 172 N. W. 514.

⁸⁵ Grandprey v. Bennett, — S. D. —, 172 N. W. 514.

⁸⁶ Bowerman v. Hamner, 250 U. S. 504, 63 L. Ed. 1113, *aff'g* McCormick v. King, 241 Fed. 737.

as indorser for money borrowed by another are not included in the computation. In such an action it is no defense that there was no improper motive nor desire for personal profit, nor that the bank in spite of such loan remained prosperous, nor that other officers or directors not sued were in part responsible, nor that the bank refrained from suing until after a change in the stockholding interest or control. The damages recoverable are those occasioned by the illegal loan and not merely the amount of the loan in excess of the limit.⁸⁷

C. Debts or Obligations for Which Officers Are Liable

§ 2660. Damages for tort and judgments therefor.⁸⁸

D. Defenses

§ 2664. Waiver, release or discharge.⁸⁹

§ 2665. Discharge of officer in bankruptcy. A bank director is an "officer" within the provision of the Bankruptcy Act excepting from discharge debts created by fraud, misappropriation or defalcation of a bankrupt while acting as an officer or in a fiduciary capacity.⁹⁰

E. Conditions Precedent

§ 2668. Necessity for judgment and execution against the corporation.⁹¹

§ 2669. Dissolution of company as condition precedent.⁹²

XXXII. REMEDIES AND PROCEDURE TO ENFORCE LIABILITY OF OFFICERS

§ 2670. Remedy as in equity or at law—In general. Where fraud of a promoter and officer is alleged, equity has jurisdiction

⁸⁷ Corsicana Nat. Bank of Corsicana v. Johnson, 251 U. S. 68, 64 L. Ed. 141.

⁸⁸ See § 2887, *infra*.

⁸⁹ Release of part of directors as release of all, see Roseville Trust Co. v. Mott, — N. J. Eq. —, 107 Atl. 462.

⁹⁰ Boyd v. Applewhite, — Miss. —, 84 So. 16.

⁹¹ Effect as against directors sought to be held personally liable, of judgment against corporation, see McCollum v. Dollar, — Tex. —, 213 S. W. 259.

⁹² See § 2630, *supra*.

of an action for an accounting.⁹³ It is proper to sue in equity although part of the relief could be obtained in an action at law.⁹⁴ Compelling a director to account for secret profits is peculiarly the province of courts of equity, and jurisdiction is not ousted because part of the relief sought could be had in an action at law.⁹⁵

An action by a creditor against the president of an insolvent corporation to compel him to pay to the corporation unlawful preferences which he had paid to other creditors, as provided for by section 90 of the General Incorporation Law of New York, is a representative suit and maintainable only in equity.⁹⁶

§ 2671. — To enforce common-law liability of officers for mismanagement, where action brought by corporation or representative if insolvent. Equity has jurisdiction of an action against directors for negligence,⁹⁷ or based on their misfeasance in fraudulently receiving corporate funds.⁹⁸ The remedy to enforce the liability of directors for making bad loans is by a suit in equity, in a proper case.⁹⁹

§ 2672. — To enforce liability created by statute. A suit against a director to enforce his statutory liability for incurring debts in excess of the prescribed capital stock is properly brought in equity.¹

§ 2675. Actions by particular persons—The corporation. A corporation may maintain an action against its officers for an accounting,² and may sue its officers and others for conspiracy

⁹³ Whitewater Tile & Pressed Brick Mfg. Co. v. Johnson, — Wis. —, 175 N. W. 786.

⁹⁴ Cahall v. Lofland, — Del. Ch. —, 108 Atl. 752.

⁹⁵ Woolson Spice Co. v. Columbia Trust Co., 110 N. Y. Misc. 687, 181 N. Y. Supp. 149.

⁹⁶ Schwartzreich v. Bauman, 112 N. Y. Misc. 464, 183 N. Y. Supp. 440.

⁹⁷ Magale v. Fomby, 132 Ark. 289, 201 S. W. 278.

⁹⁸ Keystone Guard v. Beaman, 264 Pa. 397, 107 Atl. 835.

⁹⁹ Magale v. Fomby, 132 Ark. 289, 201 S. W. 278.

¹ Boomer v. Rowe, 244 Fed. 307, rev'd on other grounds 249 Fed. 946.

That statutory liability of directors for incurring debts in excess of debt limit can be enforced only in equity, see *In re La Jolla Lumber & Mill Co.*, 243 Fed. 1004.

² Whitewater Tile & Pressed Brick Mfg. Co. v. Johnson, — Wis. —, 175 N. W. 786.

to injure the corporation, and obtain an accounting.³ An action by a corporation against its officer to recover for conversion of corporate assets is not such an election of remedies as to preclude an action against the person receiving such assets for money had and received.⁴

§ 2676. — Receiver, assignee or trustee in bankruptcy. A receiver cannot maintain an action to enforce the statutory liability of corporate officers unless he is specially so authorized by statute, according to a federal decision.⁵ So a receiver should not sue directors for corporate assets fraudulently transferred, without leave of court, they not being primary assets.⁶ A receiver cannot sue corporate officers to recover assets without leave of court, but it is not necessary for special leave where the general right to sue to reduce to money primary assets was given the receiver at the time of his appointment.⁷ A receiver will not be directed to sue promoters and directors for fraud where the probable recovery would not cover expenses.⁸ A receiver cannot enforce the statutory liability of directors for debts of the corporation, where such liability is created only in favor of creditors who became such while defendants were directors and where the debt was payable within one year or less from the time contracted.⁹ In an action by a receiver against directors for negligence in allowing embezzlements, contributory negligence of the stockholders is no defense, since the receiver represents creditors as well as stockholders.¹⁰

A trustee in bankruptcy may recover corporate funds diverted by an officer to pay private debts while the corporation was insolvent, notwithstanding many of the creditors' claims accrued after such diversion.¹¹ A trustee in bankruptcy sues not merely

³ See *National Drama Corporation v. Burns*, — N. Y. Misc. —, 183 N. Y. Supp. 739.

⁴ *Reynolds v. Union Station Bank*, 198 Mo. App. 323, 200 S. W. 711.

⁵ *Stevirmac Oil & Gas Co. v. Smith*, 259 Fed. 650.

⁶ *Cahall v. Lofland*, — Del. Ch. —, 108 Atl. 752.

⁷ *Cahall v. Lofland*, — Del. Ch. —, 108 Atl. 752.

⁸ *Du Pont v. United Oil & Fuel Co.*, — Del. Ch. —, 109 Atl. 136.

⁹ *Fordham v. Poor*, 109 N. Y. Misc. 187, 179 N. Y. Supp. 367.

¹⁰ *Besseliew v. Brown*, 177 N. C. 65, 97 S. E. 743.

¹¹ *McCullam v. Buckingham Hotel Co.*, 198 Mo. App. 107, 199 S. W. 417.

in behalf of the corporation or its stockholders but also as the representative of the creditors of the corporation, and hence he can recover corporate funds wrongfully diverted notwithstanding the ratification of such diversion by the directors and stockholders.¹² A trustee in bankruptcy cannot sue directors, in Illinois, where they had paid dividends when the company was insolvent, since the cause of action given by the statute is personal to the creditors.¹³

§ 2680. Stockholders' suits—Right of stockholder to sue in action at law. The corporation must sue rather than a stockholder where the injury is to the corporation.¹⁴ Stockholders cannot sue directors for negligence where the cause of action has passed as an asset to another corporation to whom all the property of the first corporation was conveyed.¹⁵ Negligence of directors in connection with the custody of bonds received as the purchase price of the corporate property and allotted among the stockholders in proportion to the number of shares of stock, resulting in their loss, makes the directors personally liable for such loss to the injured stockholders.¹⁶

§ 2681. — Right to sue in equity as representative of the corporation, and nature of action. A stockholders' suit against a director for negligence cannot be maintained if there is any other adequate remedy.¹⁷ An assessment on stock to remedy an impairment of capital does not preclude a stockholders' suit against the directors for negligence.¹⁸

§ 2688. Form of action at common law—In general. An action for negligence, or breach of trust, of an officer is *ex delicto* in form.¹⁹ Trover lies against the manager of a corporation for conversion of corporate money.²⁰

¹² *McCullam v. Buckingham Hotel Co.*, 198 Mo. App. 107, 199 S. W. 417.

¹³ *Seegmiller v. Day*, 249 Fed. 177.

¹⁴ *Besseliew v. Brown*, 177 N. C. 65, 97 S. E. 743.

¹⁵ *Buck v. Gimon*, 201 Ala. 619, 79 So. 51.

¹⁶ *Chadwick v. Holm*, 31 Idaho 252, 170 Pac. 87.

¹⁷ *Buck v. Gimon*, 201 Ala. 619, 79 So. 51.

¹⁸ *Harris v. Rogers*, 190 N. Y. App. Div. 208, 179 N. Y. Supp. 799.

¹⁹ *Blythe v. Enslen*, — Ala. —, 85 So. 1; *Fell v. Pitts*, 263 Pa. 314, 106 Atl. 574.

²⁰ *Moore v. Andrews*, 203 Mich. 219, 168 N. W. 1037.

§ 2689. — Action for money had and received. Where an officer appropriates corporate money to his own use, assumpsit for money had and received lies.²¹

§ 2692. Assignment of cause of action. A cause of action against directors for negligence passes to a corporation to whom all the corporate assets are conveyed.²²

§ 2697. Limitations, laches and estoppel—Whether statute runs in favor of directors or other officers. Directors are not trustees of an express trust within the rule exempting such trusts from the operation of the statute of limitations.²³ In Arkansas, directors of banks “are not trustees of an express trust within the rule exempting such trusts from the operation of the statute” but are trustees of an implied trust and are within the protection of the statute.²⁴

An action against directors for negligence is one sounding in tort so as to be barred in Alabama in one year.²⁵

§ 2701. — Period of limitations governing action to enforce penalty as applicable. A statute making officers and directors personally liable to creditors for failure to file a certificate of payment of the capital stock or for permitting the corporate debts to exceed the debt limit is not a “penal statute” within another statute fixing the time for suits or prosecutions founded upon “any penal statute.”²⁶

§ 2702. — Time when statute begins to run.²⁷ Actions against directors for negligence are barred, within the time

²¹ *Piedmont Grocery Co. v. Hawkins*, 83 W. Va. 180, 98 S. E. 152.

²² *Buck v. Gimon*, 201 Ala. 619, 79 So. 51.

²³ *Blythe v. Enslen*, — Ala. —, 85 So. 1; *Magale v. Fomby*, 132 Ark. 289, 201 S. W. 278; *Boyd v. Applewhite*, — Miss. —, 84 So. 16; *Jones Min. Co. v. Cardiff Mining & Milling Co.*, — Utah —, 191 Pac. 426.

²⁴ *Magale v. Fomby*, 132 Ark. 289, 201 S. W. 278.

²⁵ *Blythe v. Enslen*, — Ala. —, 85 So. 1.

²⁶ *Baker v. Smith*, 41 R. I. 17, 102 Atl. 721.

²⁷ Limitations as commencing to run when fraud is discovered, in action against officers for mismanagement, see *Curtis v. Metcalf*, 259 Fed. 961.

limited, after knowledge of all the facts by their successors.²⁸ In an action against corporate officers for mismanagement, limitations do not begin to run, under the Rhode Island statute, where a cause of action is fraudulently concealed, until the party entitled to sue discovers its existence.²⁹ The cause of action in favor of a corporation to recover secret profits, in a sale by a director to the corporation, accrues when the fraud is consummated by the delivery of a deed to the corporation.³⁰

§ 2704. — Laches and estoppel.³¹ A corporation or its officers are under no duty to examine public records to discover the fraud of a director in selling property to it.³²

The fact that a stockholder knew there was no periodical examination of the books of the company does not estop him to claim liability of directors for negligence in not having such an examination made.³³

§ 2706. Abatement and revival—Where action based on a statute. The statutory liability of directors for loss to stockholders from untrue statements in prospectuses or reports is a liability in tort, so far as survival of the cause of action after death of directors is concerned.³⁴

§ 2707. Parties—In general. An action under sections 90 and 91 of the General Incorporation Law can be brought only by one who is a director at the time of the bringing of the action, and this must be directly or by necessary inference stated in the complaint.³⁵

²⁸ *Curtis v. Connly*, 264 Fed. 650.

²⁹ *Curtis v. Metcalf*, 259 Fed. 961.

³⁰ *Highland Park Inv. Co. v. List*, — Cal. App. —, 184 Pac. 48.

³¹ What constitutes laches in action by corporation against directors for wrongful misappropriations, see *Jones Min. Co. v. Cardiff Mining & Milling Co.*, — Utah —, 191 Pac. 426.

³² *Highland Park Inv. Co. v. List*, — Cal. App. —, 184 Pac. 48.

³³ *Boulicault v. Oriel Glass Co.*, — Mo. —, 223 S. W. 423.

³⁴ *Geipel v. Peach*, [1917] 2 Ch. Div. 108.

³⁵ *Rothbart v. Star Wet Wash Laundry Co.*, 185 N. Y. App. Div. 807, 174 N. Y. Supp. 76.

§ 2709. — Corporation as proper or necessary defendant. The corporation and the officer or agent committing the tort may be joined as defendants.³⁶ Where a director sues under sections 90 and 91 of the New York General Corporation Law to compel directors and officers to account for property converted, the corporation is a necessary defendant but its joinder does not make the complaint state an additional cause of action.³⁷

A bank is not liable in damages for interposing successfully an answer in an action brought against directors for misconduct, in which the bank was made a party on refusing to itself sue, and in which action it set up that plaintiff was not entitled to recover on stock purchased of a delinquent director.³⁸

§ 2710. — Joinder of all of directors or guilty parties as defendants. Directors are both jointly and severally liable for breach of trust.³⁹ All or part of the directors may be joined as defendants in an action against them for negligence or the like.⁴⁰ In suing to enforce the statutory liability of officers, one or all of the joint participants may be sued.⁴¹ For non-feasance directors liable are entitled to contribution from each other, and hence all the directors participating must be joined as defendants.⁴² In an action against officers for an accounting, the transferee of part of the diverted assets is properly made a party defendant.⁴³

§ 2712. — Receiver as necessary defendant. A receiver is not a necessary party to a suit by creditors against corporate officers sought to be held individually liable.⁴⁴

§ 2715. Multifariousness and misjoinder of causes of action. Common-law and statutory liability of directors may be asserted

³⁶ *Cotton v. Fisheries Products Co.*, 177 N. C. 56, 97 S. E. 712.

³⁷ *Higgins v. Applebaum*, 183 N. Y. App. Div. 527, 170 N. Y. Supp. 228.

³⁸ *Harris v. State Bank*, — N. Y. Misc. —, 177 N. Y. Supp. 545.

³⁹ *Fell v. Pitts*, 263 Pa. 314, 106 Atl. 574.

⁴⁰ *Curtis v. Metcalf*, 265 Fed. 293.

⁴¹ *Corsicana Nat. Bank of Corsicana v. Johnson*, 251 U. S. 68, 64 L. Ed. 141.

⁴² *Hough v. Commercial Wheat Growers Co.*, 212 Ill. App. 306.

⁴³ *Brock v. Poor*, 174 N. Y. Supp. 186.

⁴⁴ *Parsons v. Rinard Grain Co.*, 186 Iowa 1017, 173 N. W. 276.

in one bill of complaint.⁴⁵ An action by stockholders against officers for an accounting states but one cause of action although it touches them in different ways and different degrees.⁴⁶ No hard and fast rule can be laid down as what may be incorporated in a complaint in stockholders' actions, or in any action, for an accounting, where it is alleged that the corporation officers have been derelict and have mismanaged the corporation's affairs and have wrongfully appropriated the corporation's property; but "wrongful acts, if charged against the same individuals, may, as a rule, be incorporated into one statement in the complaint, regardless of how numerous or how involved the alleged wrongs may be."⁴⁷ A bill by a receiver against directors which charges fraud in dealing with the corporate property is not multifarious although defendants did not join in each transaction and were not concerned to the same extent.⁴⁸

A complaint in an action by a trustee in bankruptcy of a corporation whose existence has terminated, against certain persons who composed the board of directors and who conducted the business after the corporate existence had terminated but who took no steps to wind up the business, does not improperly join causes of action whether the action is deemed one against trustees and those to whom property has been transferred, under section 35 of the General Corporation Law, or against directors under section 91a of the General Corporation Law, where all the defendants united in the unlawful common purpose of carrying on business after the expiration of the charter.⁴⁹

§ 2716. Pleading.⁵⁰

⁴⁵ *Bowerman v. Hamner*, 250 U. S. 504, 63 L. Ed. 1113, aff'g *McCormick v. King*, 241 Fed. 737.

Charges of statutory and of common-law negligence may be joined in one bill by a receiver against directors for mismanagement. *Curtis v. Metcalf*, 259 Fed. 961.

⁴⁶ *Brock v. Poor*, 174 N. Y. Supp. 186.

⁴⁷ *Blake v. Boston Development Co.*, 50 Utah 347, 167 Pac. 672.

⁴⁸ *Cahall v. Lofland*, — Del. Ch. —, 108 Atl. 752.

⁴⁹ *Wilson v. Brown*, 107 N. Y. Misc. 167, 175 N. Y. Supp. 688.

⁵⁰ Sufficiency of complaint in action by receiver of a national bank against directors to recover losses from making loans in excess of the statutory limit and from making improvident loans, see *Curtis v. Metcalf*, 265 Fed. 293.

Sufficiency of bill alleging neg-

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§ 2719. Evidence. The adjudication in bankruptcy, including the list of claims, is admissible in an action to enforce the liability of a director.⁵¹

§ 2720. Counterclaim and set-off. An action against a director to enforce his personal liability for breach of trust, sounds in tort, so that a set-off sounding in contract cannot be interposed.⁵²

§ 2722. Decree, damages recoverable and incidental relief.⁵³ Where an accounting is sought, a decree may be rendered against the officers of the corporation as well as the corporation.⁵⁴ Directors cannot be subjected to punitive damages for passing a legal resolution doing no actual damage to the complaining party, regardless of their motives in so doing.⁵⁵ Corporate officers may be held liable for profits lost by mismanagement, based on past profits, in case of an established business, under proper management.⁵⁶

XXXIII. CRIMINAL LIABILITY AND PENALTIES

§ 2724. General rules.⁵⁷ A corporate officer cannot escape criminal liability on the ground that the act was an official one as representative of the corporation.⁵⁸ Corporate agencies cannot shield themselves behind the corporation where they are the actual and efficient actors in committing a fraud or other

ligence and fraud of corporate officers, to state cause of action, see *Hawkins v. Clay County Cotton Oil Co.*, — Miss. —, 86 So. 291.

Sufficiency of bill against director and president for an accounting of profits made by him which belonged to the corporation, see *State ex rel. Smalley v. Reynolds*, 275 Mo. 113, 204 S. W. 1093.

⁵¹ *Fell v. Pitts*, 263 Pa. 314, 106 Atl. 574.

⁵² *Fell v. Pitts*, 263 Pa. 314, 106 Atl. 574.

⁵³ Form of decree in action against officers who have de-

frauded company, see *Proctor v. Farrar*, — Mo. —, 213 S. W. 469.

⁵⁴ *Sherwin v. American Loan & Investment Co.*, — N. D. —, 173 N. W. 758.

⁵⁵ *Hammond v. Sully*, 48 App. Cas. (D. C.) 320, 4 A. L. R. 160.

⁵⁶ *Goodwin v. Milwaukee Lithographing Co.*, — Wis. —, 177 N. W. 618.

⁵⁷ Criminal liability of treasurer for forgery and larceny, and defenses, see *Com. v. Peakes*, 231 Mass. 449, 121 N. E. 420.

⁵⁸ *State v. Cooley*, 141 Tenn. 33, 206 S. W. 182.

criminal offense.⁵⁹ A person indicted for crime as a particular officer of a corporation is estopped to deny that there was such a de jure office and that he was such officer where he had held himself out to the public as such officer for several years.⁶⁰ If one is indicted by the title which he held himself out as bearing, it is of no consequence that he is really not such officer nor that there is no such office, since he is estopped to show the truth of the matter where different from what he represented it to be to the public.⁶¹

§ 2725. Necessity for assent to or active participation of officer. A president is not criminally liable for an act of other officers or of employees, for a violation of law in the conduct of the business, unless such act is done with his knowledge.⁶² He is not criminally liable for the act of a subordinate in keeping an obscene book for sale without his knowledge.⁶³

§ 2733. Penalties.⁶⁴

⁵⁹ Kelly v. United States, 258 Fed. 392, 401.

⁶⁰ Ex parte State, 201 Ala. 59, 77 So. 353, rev'g Kramer v. State, 16 Ala. App. 40, 75 So. 185.

⁶¹ Ex parte State, 201 Ala. 59, 77 So. 353, rev'g Kramer v. State, 16 Ala. App. 40, 75 So. 185.

⁶² State v. Viviano, — Mo. App. —, 206 S. W. 235.

⁶³ People v. Brainard, 192 N. Y. App. Div. 816, 183 N. Y. Supp. 452.

⁶⁴ Construction of Pennsylvania statute imposing penalty for failure to keep stock book and have it open for inspection, see Hammond v. Aluminum Co. of America, 261 Pa. 370, 104 Atl. 660.

CHAPTER 43

COMPENSATION OF OFFICERS

- § 2734. Compensation of directors in the absence of contract.
- § 2736. Compensation of officers other than directors in absence of contract.
- § 2737. Compensation of directors who are officers in absence of contract.
- § 2738. Implied contracts to pay for services—In general.
- § 2743. Express contracts for compensation in general.
- § 2747. Power to fix compensation—Power of stockholders.
- § 2748. — Power of directors—As to salaries of directors.
- § 2750. — Compensation of officers other than directors.
- § 2751. — Power of officers.
- § 2752. — Effect of votes or presence of interested directors or officers.
- § 2753. Time of fixing compensation.
- § 2754. Manner of fixing compensation.
- § 2755. Necessity of good faith in fixing compensation.
- § 2756. Amount of compensation or salary.
- § 2758. Compensation of officers holding over.
- § 2760. Changes, increases or reductions of compensation.
- § 2761. Ratification by stockholders of acts of directors fixing or increasing compensation.
- § 2762. Compensation for past services.
- § 2763. Recovery of expenses and money advanced by officers.
- § 2764. Extra compensation to officers.
- § 2765. Rights of de facto officers to salaries.
- § 2766. Termination of right to salary or compensation.
- § 2767. Temporary suspension of work; lessening of duties; discharge of officers; resignation.
- § 2777. Actions by officers to recover salaries or compensation—Findings and questions of fact.
- § 2779. Actions to recover salaries or compensation received by officers.

§ 2734. Compensation of directors in the absence of contract.

Directors and officers serve without compensation for performing their usual and ordinary duties, in the absence of an express provision by statute, charter, by-laws or agreement.¹

¹ *Fox v. Arctic Placer Mining & Milling Co.*, — N. Y. —, 128 N. E. 154, rev'g on other grounds 185 N. Y. App. Div. 761, 173 N. Y. Supp. 708.

§ 2736. Compensation of officers other than directors in absence of contract. Neither a president and general manager,² nor a vice president,³ nor a secretary,⁴ nor the secretary and examiner of a farm loan company,⁵ is entitled to compensation for his services where not provided for by charter, by-law, resolution of the directors or other agreement.

§ 2737. Compensation of directors who are officers in absence of contract. Where a director fills, in addition, another office, he is not entitled to compensation unless expressly provided for.⁶

§ 2738. Implied contracts to pay for services—In general. Where services are rendered under such circumstances as to imply a promise to pay therefor, as where the minutes of the corporation show that certain officers were not only expecting and claiming compensation for their services but also that they had been receiving compensation from the commencement of their term of office, there is an implied promise to pay.⁷ A director who was also vice president of a mining company and who had for several years been in Alaska under a special agreement for compensation is not entitled to pay for advising and consulting with other officers on his return, in the absence of express agreement.⁸ Directors may receive compensation in the capacity of officers or employees.⁹

§ 2743. Express contracts for compensation in general.¹⁰ In a corporation where all the stockholders were directors, it was agreed that certain additional salaries be paid them as officers out of the net earnings in excess of the eight per cent dividend,

² *Fields v. Victor Building & Loan Co.*, — Okla. —, 175 Pac. 529.

³ *Fox v. Arctic Placer Mining & Milling Co.*, 180 N. Y. App. Div. 761, 173 N. Y. Supp. 708.

⁴ *Sunshine Laundry Co. v. Rhodes Ave. Hospital*, 207 Ill. App. 19.

⁵ *Welden v. Stephens Farm Loan Co.*, — Mo. —, 213 S. W. 54.

⁶ *Spalding v. Enid Cemetery Ass'n*, — Okla. —, 184 Pac. 579.

⁷ *Spalding v. Enid Cemetery Ass'n*, — Okla. —, 184 Pac. 579.

⁸ *Fox v. Arctic Placer Mining & Milling Co.*, 185 N. Y. App. Div. 761, 173 N. Y. Supp. 708.

⁹ *Sotter v. Coatesville Boiler Works*, 257 Pa. 411, 101 Atl. 744.

¹⁰ Construction as to amount, see § 2756, *infra*.

in proportion to their holdings of stock in the company. It was held that this was not invalid as amounting to a dividend of excess profits between stockholders of the same class, not according to the amount of stock each one owns.¹¹

§ 2747. Power to fix compensation—Power of stockholders.¹²

§ 2748. — Power of directors—As to salaries of directors. Directors, acting as such at their meetings, have no power to vote themselves salaries or compensation for their services, either before or after such services have been rendered.¹³

§ 2750. — Compensation of officers other than directors. An individual member of the board, as distinguished from the board, cannot agree to pay an officer for services.¹⁴ The board of directors have authority to order the transfer of stock held in a subsidiary corporation, to an officer of the company, for payment in organizing the subsidiary.¹⁵

§ 2751. — Power of officers. The president cannot himself arbitrarily increase his salary.¹⁶ Officers selling stock in violation of the by-laws cannot pay themselves salaries or commissions.¹⁷

§ 2752. — Effect of votes or presence of interested directors or officers. Directors cannot vote themselves compensation for past services where a majority voting therefor are pecuniarily interested.¹⁸ So voting an increase of salary is voidable where the vote of the officer whose salary is increased is needed to carry the resolution of the board of directors.¹⁹ A resolution

¹¹ *Foster v. C. G. Howes Co.*, 230 Mass. 43, 119 N. E. 356.

¹² Necessity for fixing amount in by-laws, see § 2753, *infra*.

¹³ *Palmer v. Scheftel*, 183 N. Y. App. Div. 77, 170 N. Y. Supp. 588.

¹⁴ *Fox v. Arctic Placer Mining & Milling Co.*, 185 N. Y. App. Div. 761, 173 N. Y. Supp. 708.

¹⁵ *Batchellor v. Olmsted*, 261 Fed. 533.

¹⁶ *McCullam v. Buckingham Hotel Co.*, 198 Mo. App. 107, 199 S. W. 417.

¹⁷ *Taylor v. Citizens' Oil Co.*, 182 Ky. 350, 206 S. W. 644.

¹⁸ *Wonderful Group Min. Co. v. Rand*, — Wash. —, 191 Pac. 631.

¹⁹ *Atwater v. Elkhorn Valley Coal Land Co.*, 184 N. Y. App. Div. 253, 171 N. Y. Supp. 552.

fixing the salary of the president is void where of the five directors only three were present and voted, one of them being the president himself.²⁰

The rule that directors cannot vote themselves compensation cannot be evaded by voting separately on the compensation for each director who was also an executive officer, and having the director whose compensation is voted on refrain from voting, where a majority of those voting have a pecuniary interest in the general plan.²¹

§ 2753. Time of fixing compensation. The mere omission to fix the salary of officers in the by-laws does not deprive them of the right to compensation.²²

§ 2754. Manner of fixing compensation. Where two persons practically own a corporation, they may informally agree on the salary to be paid to each.²³

§ 2755. Necessity of good faith in fixing compensation. Stockholders who are also directors cannot appropriate to their own private ends, by way of salaries, all the earnings of the company.²⁴

§ 2756. Amount of compensation or salary.²⁵ Compensation of officers for performing a certain act must be reasonable.²⁶ A corporation may contract with its manager to pay him half

²⁰ *Fields v. Victor Building & Loan Co.*, — Okla. —, 175 Pac. 529.

²¹ *Wonderful Group Min. Co. v. Rand*, — Wash. —, 191 Pac. 631, approving *Mallory v. Mallory-Wheeler Co.*, 61 Conn. 131, 23 Atl. 708.

²² *Spalding v. Enid Cemetery Ass'n*, — Okla. —, 184 Pac. 579.

²³ *Hyman v. Karl Stern Co.*, — Cal. App. —, 191 Pac. 47.

²⁴ *Townsend v. Winburn*, 107 N. Y. Misc. 443, 177 N. Y. Supp. 757.

²⁵ Construction of contract between corporation and its manager under which he was to have

certain stock put in escrow for him after payment "of the debts for 1912," see *Wright v. Barnard*, 248 Fed. 756.

Construction of contract where by president was to have percentage of net earnings of railway department, see *Bettendorf v. Bettendorf*, — Iowa —, 179 N. W. 444.

²⁶ *Proctor v. Farrar*, — Mo. —, 213 S. W. 469.

Commissions charged by a director for selling land of the corporation must be fair and reasonable. *Jordan v. Jordan Co.*, — Conn. —, 109 Atl. 181.

of the net profits of a branch of the business, although the other branch might operate at a loss.²⁷ If a contract with a sales manager, providing for payment of commissions, calls for a drawing account of \$8,500 a year in addition to expenses, he is entitled to at least such \$8,500, on breach of the contract.²⁸ If the secretary, without objection, performs the duties of general manager, he is at least entitled to the salary the corporation had agreed to pay him as secretary.²⁹ A railroad company has power to agree with its chief clerk at a point on the Canadian line that he should remit to the railroad all fees received as customs broker for the United States.³⁰

"Net profits," as used in a contract giving a certain per cent thereof to the manager as his compensation, includes the appreciation in value of the corporation's assets during the year, it was held in a particular case, where the company was a trading corporation.³¹

§ 2758. Compensation of officers holding over. Officers re-elected are presumed to have the same compensation as before.³²

§ 2760. Changes, increases or reductions of compensation. Salaries of officers cannot be altered, during the term of office, by the board of directors, without the consent of such officers.³³

§ 2761. Ratification by stockholders of acts of directors fixing or increasing compensation. Prohibiting payment of directors unless passed or confirmed at a general meeting of stockholders does not prohibit granting a director reasonable compensation for acting as traveling salesman without such authority.³⁴

²⁷ Moore v. Andrews, 203 Mich. 219, 168 N. W. 1037.

²⁸ Primos Chemical Co. v. Fulton Steel Co., 266 Fed. 937.

²⁹ Illinois State Bank v. Queen City Quarry Co., 203 Ill. App. 176.

³⁰ Duluth, S. S. & A. R. Co. v. Wilson, 200 Mich. 313, 167 N. W. 55.

³¹ Cuneo v. Giannini, — Cal. App. —, 180 Pac. 633.

Meaning of "net profits" in contract of employment of manager, see Patent Castings Syndicate, Ltd. v. Etherington, [1919] 2 Ch. Div. 254; S. J. & E. Fellows, Ltd. v. Corker, [1918] 1 Ch. Div. 9.

³² Fisher v. Massillon Iron & Steel Co., 209 Ill. App. 616.

³³ Fisher v. Massillon Iron & Steel Co., 209 Ill. App. 616.

³⁴ Canada Bonded Attorney &

§ 2762. Compensation for past services. Payments to corporate officers or directors, for past services rendered, are improper, as against corporate creditors, where there was no agreement for compensation.³⁵ Back salaries for a year should not be paid corporate officers where there was no agreement, express or implied, for a salary.³⁶ A gift of corporate property by directors to a retiring director is illegal, regardless of the purpose for which it was to be applied, i.e., as payment of a balance due on a stock subscription.³⁷ It has been held, however, that a religious society may deed land to its pastor in recognition of past services.³⁸

§ 2763. Recovery of expenses and money advanced by officers. An officer is not entitled to reimbursement for money spent for the corporation without authority, where the expenditure in no way benefited the corporation.³⁹

§ 2764. Extra compensation to officers.⁴⁰ An agreement, made by directors without consideration, to credit the president on his unpaid stock subscription with a sum equal to one month's salary, is in violation of Mass. St., c. 437, § 14.⁴¹

§ 2765. Rights of de facto officers to salaries. In an action by a bank cashier against the bank for compensation, his ineligibility because not a stockholder cannot be urged as a defense.⁴²

§ 2766. Termination of right to salary or compensation. Unfaithfulness of directors bars compensation,⁴³ and officers who

Legal Directory, Ltd. v. Leonard-Parmiter, Ltd., 42 Dom. L. Rep. (Can.) 342.

³⁵ Taylor v. Ellsworth Building Corporation, — N. Y. Misc. —, 183 N. Y. Supp. 394.

³⁶ Southwestern Portland Cement Co. v. Latta & Happer, — Tex. Civ. App. —, 193 S. W. 1115.

³⁷ Moss v. Copelof, — Mass. —, 126 N. E. 474.

³⁸ Uzzell v. McClelland, 65 Colo. 324, 176 Pac. 304.

³⁹ Interstate Investment & Development Co. v. Webster, — Iowa —, 177 N. W. 554.

⁴⁰ Bonuses for corporate officials, see article in 86 L. J. 208-211.

⁴¹ Moss v. Copelof, 231 Mass. 513, 121 N. E. 508.

⁴² Hess v. Kismet State Bank, 106 Kan. 701, 189 Pac. 919.

⁴³ Cook v. Hinds, 44 Dom. L. Rep. (Can.) 586.

use their offices for the purpose of defrauding the company out of its property are not entitled to salary.⁴⁴ A general manager is not entitled to compensation where he conspires with others to injure the corporation.⁴⁵

§ 2767. Temporary suspension of work; lessening of duties; discharge of officers; resignation. One who voluntarily vacates his office in a corporation cannot recover salary thereafter accruing.⁴⁶ Where one is given stock in consideration of giving up his position with another company and signing a contract as general manager, he is entitled to such stock although discharged prior to the termination of his contract.⁴⁷

§ 2777. Actions by officers to recover salaries or compensation—Findings and questions of fact.⁴⁸

§ 2779. Actions to recover salaries or compensation received by officers. Excessive salaries paid officers may be recovered back at the suit of minority stockholders.⁴⁹

⁴⁴ *Munro v. Smith*, 259 Fed. 1, 21.

⁴⁵ *Munro v. Smith*, 259 Fed. 1, 21.

⁴⁶ *Birmingham Realty Co. v. Hale*, 16 Ala. App. 460, 78 So. 723.

⁴⁷ *Michigan Crown Fender Co. v. Welch*, 211 Mich. 148, 178 N. W. 684.

⁴⁸ Whether vice president and

director was entitled to compensation for services rendered as a mining expert held a question of fact in *Fox v. Arctic Placer Mining & Milling Co.*, — N. Y. —, 128 N. E. 154, rev'g 185 N. Y. App. Div. 761, 173 N. Y. Supp. 708.

⁴⁹ *Atwater v. Elkhorn Valley Coal Land Co.*, 184 N. Y. App. Div. 253, 171 N. Y. Supp. 552.

CHAPTER 44

CORPORATE BOOKS AND RECORDS

- § 2782. As public records.
- § 2784. Duty to keep books and records—Records and minute books.
- § 2787. Form and requisites—Minutes.
- § 2788. — Stock book.
- § 2790. Custody of books and records—Proper place.
- § 2793. Books and records as evidence—As best evidence.
- § 2796. — Parol evidence of corporate acts.
- § 2800. Authentication of books and records.
- § 2801. Purposes for which and actions in which books and records admissible—In general.
- § 2803. — Actions between corporation or members and strangers.
- § 2805. Production of books and papers in court.
- § 2808. False entries in books.

§ 2782. **As public records.** Corporate records are not public unless a statute obliges the corporation to expose them to public inspection.¹

§ 2784. **Duty to keep books and records—Records and minute books.** A record of corporate resolutions is not essential to their validity.²

§ 2787. **Form and requisites—Minutes.** Minutes of a corporate meeting are not sufficient to satisfy the statute of frauds, as against a stockholder who did not sign them, although signed by the secretary, where he signed merely as the agent of the corporation.³

§ 2788. — **Stock book.** The statutory right of inspection imposes on the corporation the duty of keeping its stock sub-

¹ Carlton v. Camfield, — Colo. —, 171 Pac. 1140.

³ Asbury v. Mauney, 173 N. C. 454, 92 S. E. 267.

² Bank of Napa v. Ferguson Burns Estate, — Cal. App. —, 192 Pac. 66.

scriptions and accounts in such form that they may be examined and the condition of the corporate affairs ascertained therefrom, since otherwise the right of inspection is a barren legal right and of no value.⁴

§ 2790. Custody of books and records—Proper place. A mandatory injunction has been held proper to require a corporation to return its records to the home state and to keep them in the state for inspection.⁵ In Maine, a nonresident corporation is required to keep books at some fixed place, showing a complete list of all stockholders.⁶

§ 2793. Books and records as evidence—As best evidence.⁷ The fact that a certain ledger is an official book of a corporation does not preclude the admission of other corporate books which will throw light on the true state of an account in issue.⁸ Acts of directors may be shown by what they did thereafter as well as by subsequent minutes of the board.⁹

§ 2796. — Parol evidence of corporate acts.¹⁰

§ 2800. Authentication of books and records. Corporate books are sufficiently identified, to be admissible in evidence, where identified by the first secretary of the corporation.¹¹

§ 2801. Purposes for which and actions in which books and records admissible—In general.¹² Corporate books are prima facie evidence against the corporation and its directors.¹³ Cor-

⁴ *Dunn v. Acme Auto & Garage Co.*, 168 Wis. 128, 169 N. W. 297.

⁵ *Baillie v. Columbia Gold Min. Co.*, 86 Ore. 1, 166 Pac. 965, 167 Pac. 1167.

⁶ *Bryer v. Wyman*, 118 Me. 378, 108 Atl. 331.

⁷ See generally § 3095 et seq., *infra*.

Parol evidence of incorporation, see § 425, *supra*.

⁸ *Sheatz v. Markley*, 249 Fed. . Atl. 574. 315.

⁹ *Martin v. Cushwa*, — W. Va. —, 104 S. E. 97.

¹⁰ See § 3100, *infra*.

¹¹ *Zierath v. Claggett*, — Cal. App. —, 188 Pac. 837.

¹² Minutes of directors as showing account stated, see *Parker v. Merchants' & Insurers' Reporting Co.*, — Cal. App. —, 186 Pac. 192.

Stock book as evidence, see *Lowery v. Mutual Loan Society*, 202 Ala. 51, 79 So. 389.

¹³ *Fell v. Pitts*, 263 Pa. 314, 106

porate records are evidence against the company to show want of intent to employ real estate in its business.¹⁴ A minute book kept by the directors is admissible against a stockholder to show the powers conferred on the cashier.¹⁵ Directors are chargeable with knowledge of what transpires at directors' meetings, and the directors' minute book is evidence against them as to what they did at those meetings.¹⁶

§ 2803. — Actions between corporation or members and strangers. Recitals in corporate minutes are self-serving declarations not admissible against third persons.¹⁷

§ 2805. Production of books and papers in court. In determining the propriety of an order to produce corporate books at the trial, the rights of a stockholder ordinarily are not considered.¹⁸ Corporation records may be taken by a search warrant although the records may be evidence against the corporation in a criminal case.¹⁹ The rights of a corporation against unlawful search and seizure of papers are to be protected even if the same result might have been achieved in a different lawful way.²⁰ A corporation cannot be compelled to produce its books and papers for use in a criminal proceeding against it, where based on information obtained through a previous unconstitutional search and seizure.²¹

§ 2808. False entries in books. Entries in the books of a corporation are not evidence, where sham and fictitious.²²

¹⁴ *Com. v. Clark County Nat. Bank*, 187 Ky. 151, 219 S. W. 175.

¹⁵ *Choctaw Bank v. Gewin*, 16 Ala. App. 349, 78 So. 96.

¹⁶ *Johnson v. Canfield-Swigart Co.*, 292 Ill. 101, 126 N. E. 608, aff'g 211 Ill. App. 423.

¹⁷ See § 3101, *infra*.

¹⁸ *Subers v. Continental Securities Co.*, — Del. Ch. —, 111 Atl. 433.

¹⁹ *In re Rosenwasser Bros.*, 254 Fed. 171.

²⁰ *Silverthorne Lumber Co. v. United States of America*, 251 U. S. 385, 64 L. Ed. 319.

²¹ *Silverthorne Lumber Co. v. United States of America*, 251 U. S. 385, 64 L. Ed. 319.

²² *Axford v. Western Syndicate Inv. Co.*, 141 Minn. 412, 170 N. W. 587.

CHAPTER 45

INSPECTION OF CORPORATE BOOKS AND RECORDS

I. SOURCES OF RIGHT OF INSPECTION

- § 2810. Right at common law.
- § 2811. Constitutional and statutory provisions—In general.
- § 2812. — Extent of stockholder's interest.
- § 2813. By-laws providing for inspection.

II. PURPOSES FOR WHICH ALLOWED

- § 2814. In general.
- § 2815. Effect of statutes as to inspection.
- § 2817. Relation between inspection and interest of stockholder.
- § 2818. Investigation of corporate affairs—In general.
- § 2819. — For purpose of suit by stockholder.
- § 2820. Ascertainment of value of stock.
- § 2822. Improper or unlawful purposes.

III. CORPORATIONS SUBJECT TO RIGHT

- § 2824. In general.
- § 2825. Foreign corporations.

IV. DEMAND AND REFUSAL OF INSPECTION

- § 2826. Demand.
- § 2827. Refusal.

V. BY WHOM INSPECTION MADE

- § 2830. Stockholders and agents—In general.
- § 2831. — Public accountants and stenographers.
- § 2832. Personal representatives.
- § 2834. Directors.

VI. EXTENT AND METHOD

- § 2837. In general.
- § 2840. Copying from books.
- § 2842. Abuse of right.

VII. ENFORCEMENT OF RIGHT

§ 2844. *Mandamus*—In general.

§ 2845. — Nature of proceeding; jurisdiction; parties.

§ 2846. — Pleading.

§ 2847. — Awarding relief.

§ 2849. Remedies in equity.

VIII. DAMAGES AND PENALTIES

§ 2851. Statutory penalties.

I. SOURCES OF RIGHT OF INSPECTION

§ 2810. Right at common law. A stockholder is entitled to inspect the corporate books and records, where he proceeds with a proper motive.¹ The fact that a corporation makes annual reports of its financial condition is no bar to an application for inspection of the books to ascertain the book value of the stock.²

§ 2811. Constitutional and statutory provisions—In general. The Maine statute provides that the corporate records and stockbook “shall be open at all reasonable hours to the inspection of persons interested, who may take copies and minutes therefrom of such parts, as concern their interests.” This statute, so far as the right of inspection is concerned, adds to the common-law rights of a stockholder and removes some of the common-law limitations, and gives the stockholder an absolute and unlimited right to inspect the corporate records and the list of stockholders.³

¹ *Webster v. Bartlett Estate Co.*, 35 Cal. App. 283, 169 Pac. 702; *State ex rel. Linihan v. United Brokerage Co.*, — Del. —, 101 Atl. 433; *Pfirman v. Success Min. Co.*, 30 Idaho 468, 166 Pac. 216; *Feick v. Hill Bread Co.*, 91 N. J. L. 486, 103 Atl. 813; *In re Wygant*, 101 N. Y. Misc. 509, 167 N. Y. Supp. 369; *Com. v. Pennsylvania Silk Co.*, — Pa. —, 110 Atl. 157.

² *Feick v. Hill Bread Co.*, 91 N. J. L. 486, 103 Atl. 813.

³ *Knox v. Coburn*, 117 Me. 409,

104 Atl. 788, citing *Eaton v. Manter*, 114 Me. 260, 95 Atl. 948; *Withington v. Bradley*, 111 Me. 386, 89 Atl. 201; *White v. Manter*, 109 Me. 409, 42 L. R. A. (N. S.) 332, 84 Atl. 890. See also § 2815, *infra*.

The statute in Maine requiring corporations to permit inspection of their books applies, although the corporation has a treasurer's office at a fixed place in the state where a stock book is kept. *Bryer v. Wyman*, 118 Me. 378, 108 Atl. 331.

§ 2812. — **Extent of stockholder's interest.** A registered holder of stock who is under contract to sell it cannot compel an inspection of corporate books.⁴

§ 2813. **By-laws providing for inspection.** If a statute permits inspection of corporate books, "under such regulations as may be prescribed by the by-laws," a by-law cannot limit the right of inspection to only a part of the books.⁵

II. PURPOSES FOR WHICH ALLOWED

§ 2814. **In general.** An application not made in good faith may be denied, in the absence of any statute.⁶

§ 2815. **Effect of statutes as to inspection.** The California statute, at least prior to the 1917 amendment, gave an absolute right to inspection without regard to the motives of the applicant.⁷ In 1917 California amended its statute (Civ. Code Calif. §§ 377, 378) by providing that "the board of directors may, by unanimous vote, deny such examination or inspection to a stockholder who demands the same with intent to use to the injury of the corporation the information to be acquired thereby, and a satisfactory showing of such intent shall be a complete defense to any action or proceeding brought by any such person to compel the officers of any such corporation to submit any of such records for his inspection or examination." In addition, in regard to the stock and transfer book, the statute which provided that it must be kept open to the inspection of "any stockholder, member or creditor" was amended in 1917 so as to read that it shall be open to inspection "of any officer, bona fide stockholder, member, or creditor of the corporation."

The right given by the Colorado statutes to inspect the stock ledger and list of stockholders is an absolute one so that the motive of the applying stockholder cannot be inquired into.⁸

⁴In re Gaines, — N. Y. Misc. —, 180 N. Y. Supp. 191.

⁵State ex rel. Smalley v. Sterns Tire & Tube Co., — Mo. App. —, 202 S. W. 459.

⁶In re Wygant, 101 N. Y. Misc. 509, 167 N. Y. Supp. 369.

⁷Webster v. Bartlett Estate Co., 35 Cal. App. 283, 169 Pac. 702.

⁸Jameson v. Hanawalt, — Colo. —, 186 Pac. 717; Wire v. Fisher, — Colo. —, 185 Pac. 469, holding it immaterial that the purpose was

The Idaho statute makes this right of inspection absolute.⁹

The right of examination conferred by the Illinois statutes "is unqualified and unrestricted, except, only, for the limitation that the right shall be exercised at reasonable times."¹⁰ Under the Illinois statutes giving an absolute right to inspect, it is no defense that the applicant is interested in a competing corporation and has displayed a hostile attitude towards the defending company and its officers and that by such examination he may be able to obtain information that will be of benefit to the rival company.¹¹

Under the Maine statutes, the motive in seeking inspection is immaterial, although "the character of the remedy sought by application for a writ of mandamus, and the discretion to be exercised by the court in issuing it, seems not to have been taken away or abridged by the statute," and "a state of facts might be presented where the purpose of the petitioner was so obviously vexatious, improper or unlawful that the court might feel compelled to exercise its discretion and decline to issue the writ."¹² Even though a statute makes the right of inspection absolute and unconditional, it is held in Maine that since mandamus is a discretionary writ the court "will not exercise its extraordinary power at the mere behest of one who acquires a nominal stock interest for the sole purpose of advertising other goods or stocks."¹³

The Massachusetts statute of 1903 authorizing stockholders to examine stock and transfer books is mandatory and confers

a private one wholly independent and outside of his interests as a stockholder.

A stockholder's purpose in examining corporate books is immaterial. *Jameson v. Hanawalt*, — Colo. —, 186 Pac. 717.

⁹ *Pfirman v. Success Min. Co.*, 30 Idaho 468, 166 Pac. 216.

¹⁰ *Furst v. W. T. Raleigh Medical Co.*, 282 Ill. 366, 118 N. E. 763, aff'g 205 Ill. App. 82; *Baird v. King*, 213 Ill. App. 228.

¹¹ *Furst v. W. T. Raleigh Medical Co.*, 282 Ill. 366, 118 N. E. 763, aff'g 205 Ill. App. 82.

¹² *Knox v. Coburn*, 117 Me. 409, 104 Atl. 789, and see § 2811, *supra*.

The Maine statute as to inspection makes absolute and unqualified the right which at common law was conditional. *Shea v. Sweetser*, — Me. —, 111 Atl. 579.

¹³ *Shea v. Sweetser*, — Me. —, 111 Atl. 579, where person bought five shares of stock to obtain a list of the stockholders for the purpose of attempting to sell them other stock.

unlimited rights; and thereunder it is improper to refuse a stockholder who is a broker the right to make copies and memoranda of the list of stockholders, for use in his business as a broker.¹⁴

In North Dakota, after holding the statute as to inspection mandatory regardless of the motive of the stockholders the Supreme Court reversed itself and held that mandamus should be refused where the motive is to injure the corporation unless it buys the stock of the petitioner, at least in so far as inspection by an attorney for petitioner is concerned where he had before effected a sale through threats of inspection, etc.¹⁵

In Washington, it is said that the statutory or by-law right of inspection "may not be abridged or denied, except in protection of necessary trade secrets, or to combat some evil purpose," such as the theft or destruction of records;¹⁶ and a stockholder, who was an active business competitor, was held entitled only to an inspection of the stock book, apparently on the theory that the statute gave him an absolute right to inspection of that book, while as to the other records there was no statute authorizing an inspection and hence it was proper to refuse an inspection as to them because of the bad faith of the applicant.¹⁷

§ 2817. Relation between inspection and interest of stockholder. The Maine statutes authorize an inspection by "persons interested" and the taking of copies of such parts "as concern their interest"; and it is held thereunder that a list of stockholders concerns a stockholder's interest, and that he has a right to take a copy of the list.¹⁸

§ 2818. Investigation of corporate affairs—In general. An inspection to enable a stockholder to consult with other stockholders, and obtain proxies to be used to obtain a new management, must be allowed.¹⁹

¹⁴ *Shea v. Parker*, — Mass. —, 126 N. E. 47, holding statute does not apply to the general books of account of the corporation.

¹⁵ *Lien v. Savings, Loan & Trust Co.*, — N. D. —, 174 N. W. 621, overruling *Schmidt v. Anderson*, 29 N. D. 262, 150 N. W. 871.

¹⁶ *State ex rel. Beaty v. Guarante*

tee Mfg. Co., 103 Wash. 151, 174 Pac. 459.

¹⁷ *State ex rel. Beaty v. Guarantee Mfg. Co.*, 103 Wash. 151, 174 Pac. 459.

¹⁸ *Knox v. Coburn*, 117 Me. 409, 104 Atl. 788.

¹⁹ *Drovin v. Lehigh Coal & Navigation Co.*, 265 Pa. 447, 109 Atl. 128.

§ 2819. — For purpose of suit by stockholder. An inspection will not be ordered where petitioner is not seeking to enforce any corporate right but instead to obtain information for personal use in a pending suit involving stock in the corporation.²⁰ An application is properly denied where the purpose of the inspection is to obtain information to use in bringing suits to annoy and harass the corporation and to injure its business.²¹

§ 2820. Ascertainment of value of stock. A stockholder has a right to inspect the books to ascertain the value of stock held by him, at least where it is a close corporation which does not issue reports.²²

§ 2822. Improper or unlawful purposes.²³ If the application is for an improper purpose, relief by mandamus will be denied.²⁴ An inspection of corporate books will not be compelled in favor of a stockholder engaged in unfair competition with the corporation.²⁵ A stockholder who is a broker will not be denied the right to inspect and take a copy of the list of stockholders, to be used as mailing lists in sending out circulars offering to buy or sell stock in various other corporations.²⁶

The burden of proving bad faith is on the corporation setting it up.²⁷ It will not be presumed that the motive of the stockholder is an improper one, and, if the motive or purpose is charged to be otherwise, the burden is on the officer refusing the request, or on the corporation, to establish it.²⁸

²⁰ *In re Gaines*, — N. Y. Misc. —, 180 N. Y. Supp. 191.

²¹ *State ex rel. Linihan v. United Brokerage Co.*, — Del. —, 101 Atl. 433.

²² *In re Wygant*, 101 N. Y. Misc. 509, 167 N. Y. Supp. 369.

²³ Effect of statutes, see § 2811, *supra*.

²⁴ *State ex rel. Linihan v. United Brokerage Co.*, — Del. —, 101 Atl. 433.

²⁵ *People ex rel. Giles v. Klaunder-Weldon Dyeing Mach. Co.*,

180 N. Y. App. Div. 149, 167 N. Y. Supp. 429.

²⁶ *Knox v. Coburn*, 117 Me. 409, 104 Atl. 789, following *State v. Middlesex Banking Co.*, 87 Conn. 483, 88 Atl. 861, which latter case is cited on page 4103, note 9 of the original work.

²⁷ *State ex rel. Beaty v. Guarantee Mfg. Co.*, 103 Wash. 151, 174 Pac. 459.

²⁸ *Knox v. Coburn*, 117 Me. 409, 104 Atl. 789.

III. CORPORATIONS SUBJECT TO RIGHT

§ 2824. **In general.** The right of a resident of a city to inspect the city books relating to its electric system operated by itself is closely analogous to the right of a stockholder to inspect the books of an ordinary public utility corporation.²⁹

§ 2825. **Foreign corporations.** In Missouri a statute makes every foreign corporation accepting its provisions subject to an inspection of its books at the instance of stockholders, under such regulations as are prescribed by the by-laws. It was held thereunder that the right to inspect is determined by the Missouri law rather than the law of the state where the corporation was created, and that the board of directors, by enacting by-laws, could not limit the inspection to a part only of the corporate books.³⁰

IV. DEMAND AND REFUSAL OF INSPECTION

§ 2826. **Demand.** A demand on the board of directors is not necessary before mandamus proceedings to compel the corporation and its president to permit an examination, where a demand was made on the president.³¹ A demand by the attorney for a stockholder, in his presence, is equivalent to a personal demand.³²

§ 2827. **Refusal.** Refusal to permit a stockholder to appoint his own attorney or agent to make the examination is in effect a denial of the right of inspection.³³ It is no defense to the application that the applicant has been at all times at liberty to examine the reports made by a disinterested auditor hired by the company.³⁴

²⁹ *Mushet v. Department of Public Service, City of Los Angeles*, 35 Cal. App. 630, 170 Pac. 653.

³⁰ *State ex rel. Smalley v. Sterns Tire & Tube Co.*, — Mo. App. —, 202 S. W. 459.

³¹ *Feick v. Hill Bread Co.*, 91 N. J. L. 486, 103 Atl. 813.

³² *People v. Bowie*, — N. Y. Misc. —, 166 N. Y. Supp. 905.

³³ *Pfirman v. Success Min. Co.*, 30 Idaho 468, 166 Pac. 216.

³⁴ *Furst v. W. T. Raleigh Medical Co.*, 282 Ill. 366, 118 N. E. 763, *aff'd* 205 Ill. App. 82.

V. BY WHOM INSPECTION MADE

§ 2830. Stockholders and agents—In general. A person is a stockholder entitled to inspection although he holds his stock merely as trustee and has no real or beneficial ownership, as in case of a director who holds one share of stock as trustee for another merely to qualify himself as a director.³⁵ The 1917 amendment of the California statutes restricting the right of inspection to “bona fide” stockholders is not retroactive.³⁶

§ 2831. — Public accountants and stenographers. The stockholder is entitled to the aid of expert accountants and possibly lawyers,³⁷ but is not entitled to be accompanied by the president and bookkeeper of a business rival.³⁸ Where a stockholder presents himself at the office of the company for an inspection of the stock book, the fact that his attorney is present affords no reason why he should not have his inspection.³⁹ The “weight of authority in this country appears to be that a stockholder may employ an expert accountant not connected with the corporation to assist him in making the examination,” since “the possession of the right would be futile if the possessor through the lack of knowledge necessary to its exercise were debarred of the privilege to procure in his behalf the service of one competent to exercise it”; and the corporation cannot prevent an inspection aided by outside accountants by consenting to the use of its own accountants.⁴⁰

§ 2832. Personal representatives. An executrix is entitled to inspect corporate books and to enforce such right, although not requested to do so by the creditors of the estate nor authorized by any court.⁴¹

§ 2834. Directors.⁴²

³⁵ Webster v. Bartlett Estate Co., 35 Cal. App. 283, 169 Pac. 702.

³⁶ Webster v. Bartlett Estate Co., 35 Cal. App. 283, 169 Pac. 702.

³⁷ People ex rel. Poletti v. Poletti, Coda & Rebecchi, 193 N. Y. App. Div. 738, 184 N. Y. Supp. 368; In re Wygant, 101 N. Y. Misc. 509, 167 N. Y. Supp. 369.

³⁸ People ex rel. Poletti v. Poletti, Coda & Rebecchi, 193 N. Y. App. Div. 738, 184 N. Y. Supp. 368.

³⁹ People v. Bowie, 166 N. Y. Supp. 905.

⁴⁰ Feick v. Hill Bread Co., 91 N. J. L. 486, 103 Atl. 813.

⁴¹ Feick v. Hill Bread Co., 91 N. J. L. 486, 103 Atl. 813.

⁴² See § 1991, supra.

VI. EXTENT AND METHOD

§ 2837. In general. The right of stockholders to inspect extends to correspondence concerning the business affairs of the corporation between the nonresident president who was the controlling stockholder and the vice president who had entire charge of the business.⁴³ The certificate of incorporation is a public record, so that a party is not entitled to discovery and inspection thereof.⁴⁴

§ 2840. Copying from books. The right to make copies of the records follows as an incident of the right to examine and inspect the records.⁴⁵ A stockholder may copy the list of stockholders, under the Maine statute, for use by him as a broker in sending circulars offering to buy or sell stock.⁴⁶

§ 2842. Abuse of right. The books of a going concern should not be ordered deposited in court to enforce the right of inspection except in an extreme case.⁴⁷

VII. ENFORCEMENT OF RIGHT

§ 2844. Mandamus—In general. The remedy for a denial of the right to inspect books is mandamus.⁴⁸

§ 2845. — Nature of proceeding; jurisdiction; parties. In mandamus proceedings to obtain an inspection of corporate books, the corporation is a proper party as is the president where he assumes to exercise control over the books.⁴⁹ An alternative mandamus should first be issued, and then a peremptory mandamus if there are no disputed questions of fact.⁵⁰

⁴³ *Otis-Hidden Co. v. Scheirich*, 187 Ky. 423, 219 S. W. 191.

⁴⁴ *Komow v. Simplex Cloth-Cutting Mach. Co.*, 109 N. Y. Misc. 358, 179 N. Y. Supp. 682.

⁴⁵ *Pfirman v. Success Min. Co.*, 30 Idaho 468, 166 Pac. 216.

⁴⁶ *Knox v. Coburn*, — Me. —, 104 Atl. 789.

⁴⁷ *Monte Rico Mining & Mill-*

ing Co. v. Fleming, 258 Fed. 106.

⁴⁸ *Leach v. Davy*, 199 Mich. 378, 165 N. W. 927; *Com. v. Pennsylvania Silk Co.*, — Pa. —, 110 Atl. 157.

⁴⁹ *Baird v. King*, 213 Ill. App. 228.

⁵⁰ *Com. v. Pennsylvania Silk Co.*, — Pa. —, 110 Atl. 157.

§ 2846. — **Pleading.** A petition for mandamus to compel inspection of books must allege that respondents are either corporate officers or have the custody of the books.⁵¹ The answer must be accepted as true, in Delaware.⁵² A statement in the return that the president had no authority to permit an examination is a mere conclusion of law not admitted by a demurrer to the return.⁵³

§ 2847. — **Awarding relief.** The fact that a statute makes the right of inspection absolute and unqualified does not take away or abridge the discretionary power of the court to award mandamus; the court may refuse a writ of mandamus in its discretion even where the petitioner has a clear legal right.⁵⁴

§ 2849. **Remedies in equity.**⁵⁵ A bill in equity is sometimes resorted to in order to obtain a discovery and inspection of corporate books and records, including books of account.⁵⁶ The remedy, under the Massachusetts statute of 1903, to enforce the right to inspect books, is by a suit in equity.⁵⁷

VIII. DAMAGES AND PENALTIES

§ 2851. **Statutory penalties.** In New York refusal to allow corporate books to be inspected is made a misdemeanor if the act is "wilful."⁵⁸

⁵¹ *Clark v. Tindolph*, — Colo. —, 185 Pac. 648.

⁵² *State ex rel. Linihan v. United Brokerage Co.*, — Del. —, 101 Atl. 433.

⁵³ *Feick v. Hill Bread Co.*, 91 N. J. L. 486, 103 Atl. 813.

⁵⁴ *Shea v. Sweetser*, — Me. —, 111 Atl. 579, and see § 2815, *supra*, for illustrations.

⁵⁵ Order for inspection of books

as appealable, see *Baillie v. Columbia Gold Min. Co.*, 95 Ore. 609, 188 Pac. 418.

⁵⁶ *Martin v. D. B. Martin Co.*, — Del. Ch. —, 102 Atl. 373.

⁵⁷ *Shea v. Parker*, — Mass. —, 126 N. E. 47.

⁵⁸ *People v. Bowie*, 166 N. Y. Supp. 905, holding mere prevention of inspection without any verbal refusal, a wilful refusal.

CHAPTER 46

REPORTS BY CORPORATE OFFICERS

I. STATUTORY PROVISIONS

- § 2853. Object and purpose of statutes.
- § 2854. Validity of statutes.
- § 2855. Nature and construction of statutes.

II. DUTY TO MAKE REPORTS

- § 2858. Domestic corporations.
- § 2860. Foreign corporations.
- § 2861. Excuses for failure to make and file reports.

III. FORM AND REQUISITES

- § 2863. Statement of debts.
- § 2867. Signing and verification.

IV. PUBLICATION AND FILING

- § 2870. Time of filing.

V. LIABILITY FOR NONCOMPLIANCE WITH STATUTE

- § 2874. Officers and directors who are liable.
- § 2876. Intent to disregard statute.
- § 2877. Intent to make or publish false report.
- § 2879. Debts to which liability extends—In general.
- § 2880. — As dependent upon time of contracting.
- § 2887. — Damages for torts and judgments therefor.
- § 2891. Penalties—In general.

VI. ENFORCEMENT OF LIABILITY

- § 2898. Notice of intention and judgment against corporation as prerequisite.
- § 2905. Limitation of actions.
- § 2908. Parties—Plaintiffs.
- § 2913. Pleading—Sufficiency of complaint.
- § 2920. Burden of proof.

I. STATUTORY PROVISIONS

§ 2853. Object and purpose of statutes.¹ Reports cannot be required by the state "for the avowed purpose of enabling one of its officials to do something which the Constitution forbids or, even to accomplish a proper end, in a manner prohibited by the organic law."²

Somewhat different from the statutes in other states, a statute in New York gives an absolute right to the owner of five per cent of the stock to demand a verified statement of corporate assets and liabilities, and makes the treasurer liable to penalty for failure to furnish such a statement on demand, and it is held that such right cannot be defeated by showing an improper motive nor because plaintiff is a director with daily access to the books and records.³

In Pennsylvania, the Act of 1915 requires reports both from individuals and corporations having money on deposit or property in their possession for a long time belonging to other persons, and also requires reports from every corporation of dividends or profits declared but not paid.⁴

§ 2854. Validity of statutes. The validity of a statute requiring reports by corporations may be attacked before it is attempted to be enforced by escheat.⁵

§ 2855. Nature and construction of statutes. The ordinary class of statutes are not penal in the sense in which "penal" is used in criminal law.⁶ The statutory liability in Colorado for failure to file a report is separate and distinct from the liability for a false report.⁷

II. DUTY TO MAKE REPORTS

§ 2858. Domestic corporations. The Delaware statute making it a misdemeanor to fail to file the annual report applies equally

¹ Liability in Canada for failure to make annual report, see *Seagram v. Pneuma Tubes, Ltd.*, 44 Dom. L. Rep. (Can.) 578.

² *Germantown Trust Co. v. Powell*, 260 Pa. 181, 103 Atl. 596.

³ *Klingenschmidt v. Martocci*, 108 N. Y. Misc. 626, 178 N. Y. Supp. 673.

⁴ *Germantown Trust Co. v. Powell*, 260 Pa. 181, 103 Atl. 596.

⁵ *Germantown Trust Co. v. Powell*, 260 Pa. 181, 103 Atl. 596.

⁶ *Northern Pac. R. Co. v. Crowell*, 245 Fed. 668, Montana statute.

⁷ *Schroeder v. Snarr*, — Colo. —, 189 Pac. 931.

well to corporations created by a special act.⁸ The word "charter" as used in a statute requiring the filing of a certificate as to capital stock should not be confined to corporations created by special act of the legislature so as to exclude corporations formed under general laws where there is no good reason for making such a distinction.⁹

§ 2860. Foreign corporations. By statute, directors of a foreign corporation cannot be made liable for corporate debts for failure to file annual reports, unless the statute is limited to debts incurred in the state where the statute was enacted.¹⁰ The Montana statute making directors liable for failure to file an annual report does not apply to directors of foreign corporations.¹¹

§ 2861. Excuses for failure to make and file reports.¹²

III. FORM AND REQUISITES

§ 2863. Statement of debts. An annual report filed February 28th is insufficient where it states the corporate indebtedness as of January 1st.¹³

§ 2867. Signing and verification.¹⁴

IV. PUBLICATION AND FILING

§ 2870. Time of filing. Filing a report after suit commenced to enforce the directors' liability does not affect the liability.¹⁵ The 1915 statute in Michigan as to filing reports requires filing within sixty days after the close of the corporate fiscal year and provides that directors shall be liable if they continue in default

⁸ State v. Front & U. St. Ry. Co., — Del. —, 104 Atl. 154.

⁹ Baker v. Smith, 41 R. I. 17, 102 Atl. 721.

¹⁰ Stark Bros. Nurseries & Orchards Co. v. Little, 257 Fed. 421.

¹¹ Stark Bros. Nurseries & Orchards Co. v. Little, 257 Fed. 421.

¹² See § 2876, infra.

¹³ Perini v. Continental Oil Co., — Colo. —, 190 Pac. 532.

¹⁴ Necessity for verification under Montana statute, see Minneapolis Steel & Machinery Co. v. Thomas, 54 Mont. 132, 168 Pac. 40.

¹⁵ Edmisten v. M. E. Smith & Co., — Colo. —, 185 Pac. 258.

ten days thereafter. Under it, the liability of directors does not begin until the end of the seventy day period.¹⁶

V. LIABILITY FOR NONCOMPLIANCE WITH STATUTE

§ 2874. Officers and directors who are liable. Although the statute requires the president and secretary to file the annual report, directors are liable for negligence if they knowingly permit a false report to be filed or if they fail to exercise proper diligence to see that the officers do their duty.¹⁷

§ 2876. Intent to disregard statute. In Michigan, a good faith effort to comply with the statute as to filing the annual report is a defense.¹⁸

§ 2877. Intent to make or publish false report. A director who did not sign false statements in the annual certificates of condition required by statute, with knowledge of their falsity or with reckless carelessness, is not liable to a third person with whom the director had no relations.¹⁹

§ 2879. Debts to which liability extends—In general. “Debts” for which the president of the corporation is liable, on failure to file an annual report, includes liability of a bank to a ward for a trust fund on deposit.²⁰

§ 2880. — As dependent upon time of contracting. The Colorado statute providing that if the report is not filed within sixty days after January 1st, directors shall be liable for all corporate debts contracted in the preceding year “and until such report shall be made and filed,” does not preclude liability even though no default existed when the debt was contracted and the report was filed before suit was commenced.²¹

¹⁶ *Vulcanized Products Co. v. Bender*, 202 Mich. 346, 168 N. W. 444, distinguishing *Reuter Hub & Spoke Co. v. Hicks*, 181 Mich. 250, 148 N. W. 339, as decided under an earlier statute.

¹⁷ *Bank of Commerce v. Goolsby*, 129 Ark. 416, 196 S. W. 803.

¹⁸ *Macbeth-Evans Glass Co. v.*

Gumbinsky, 201 Mich. 18, 166 N. W. 936.

¹⁹ *Beaman v. Gerrish*, — Mass. —, 126 N. E. 352.

²⁰ *Blanton v. First Nat. Bank of Forrest City*, 136 Ark. 441, 206 S. W. 745.

²¹ *Edmisten v. M. E. Smith & Co.*, — Colo. —, 185 Pac. 258.

§ 2887. — **Damages for torts and judgments therefor.** "Debts," within the meaning of the statute making corporate officers individually liable for debts in case of failure to file an annual report, must be those arising out of contract and not liability for torts.²² The Montana statute making directors liable for judgments thereafter incurred as well as for debts, for failure to file an annual report, includes liability on judgments for torts, especially since the liability on judgments was added by amendment of the statute and no amendment would have been necessary if it was not intended to include torts.²³

§ 2891. **Penalties—In general.**²⁴ Statutes in some states penalize in a fixed sum the failure to file reports.²⁵ The fact that failure to file the report in no way prejudiced or misled plaintiff as to the condition of the corporation, while not controlling, is of some significance in determining whether the statute makes imposition of the prescribed penalty imperative.²⁶

VI. ENFORCEMENT OF LIABILITY

§ 2898. **Notice of intention and judgment against corporation as prerequisites.** Directors are bound by a judgment for a tort against the corporation, so far as liability thereon for failure to file the annual report is concerned, in Montana.²⁷

§ 2905. **Limitation of actions.** The statute of Montana which specifically fixes the time to sue directors to recover a penalty imposed by statute governs in an action in another state, instead of the law of the forum.²⁸ The fact that directors, by failing

²² *Blanton v. First Nat. Bank of Forrest City*, 136 Ark. 441, 206 S. W. 745, applying rule where bank knowingly credited personal account of guardian on deposit of ward's money.

²³ Liability for "all debts or judgments" includes judgment for a tort. *Northern Pac. R. Co. v. Crowell*, 245 Fed. 668, 677.

²⁴ Action by state for failure to file annual reports, see *State ex*

rel. Coco v. Union Gas, Oil & Pipe Line Co., 147 La. 701, 85 So. 645.

²⁵ *State ex rel. Coco v. Farmer-ville Light & Power Co.*, 144 La. 241, 80 So. 268.

²⁶ *Macbeth-Evans Glass Co. v. Gumbinsky*, 201 Mich. 18, 166 N. W. 936.

²⁷ *Northern Pac. R. Co. v. Crowell*, 245 Fed. 668, 676.

²⁸ *Northern Pac. R. Co. v. Crowell*, 245 Fed. 668.

to file a report, have become subject to the statutory penalty, and the period of one year has elapsed after the right to a penalty has accrued, does not bar an action for failure to file a report for a subsequent year.²⁹

§ 2908. Parties—Plaintiffs. An assignee of a creditor may sue directors for failure to make the annual report.³⁰

§ 2913. Pleading—Sufficiency of complaint. In Colorado, a complaint against directors is insufficient where it does not show whether the default was in failing to file any report, filing an insufficient report, or filing a false report.³¹

§ 2920. Burden of proof. The burden of proving that the report was not filed on time is on plaintiff.³²

²⁹ Perini v. Continental Oil Co., — Colo. —, 190 Pac. 532.

³⁰ Perini v. Continental Oil Co., — Colo. —, 190 Pac. 532, following Credit Men's Adjustment Co. v. Vickery, 62 Colo. 214, Ann. Cas. 1918 E 1074, 161 Pac. 297.

³¹ Schroeder v. Snarr, — Colo. —, 189 Pac. 931.

³² Minneapolis Steel & Machinery Co. v. Thomas, 54 Mont. 132, 168 Pac. 40.

CHAPTER 47

ACTIONS BY AND AGAINST CORPORATIONS

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- § 3104. Admissions and declarations by officers, agents and stockholders.
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- § 3106. — Corporate existence, incidents and character.
- § 3108. Witnesses in action where corporation is party—Competency where interest of a decedent is adverse.
- § 3109. Subpoenas and notices to produce or to allow inspection.
- § 3110. Discovery, inspection and examination or deposition.

VII. TRIAL AND ITS INCIDENTS

- § 3112. In general.
- § 3113. Conduct and control; compromise and discontinuance.
- § 3114. Judge and jury.

VIII. JUDGMENT AND ENFORCEMENT; APPEAL AND REVIEW

§ 3119. Defaults and confessions.

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§ 3123. Amendment, vacation or other relief from judgment.

§ 3124. Conclusiveness and effect; collateral attack.

§ 3125. Appeal and review.

I. POWER AND CAPACITY FOR LITIGATION; RIGHTS OF ACTION AND DEFENSE

§ 2925. In general; corporation as distinct party.¹ An action for goods sold by a corporation cannot be brought in the name of the person who had incorporated the business several months before the sale.² A corporation had power to sue, during the war with Germany, although nearly all its stockholders were alien enemies living in Germany at the time of the war, especially where a majority of the directors, including its managing director, were residents of this country at the time.³

§ 2926. Rule at common law; assimilation to natural persons. An athletic association incorporated through a pro forma decree has the power to sue.⁴

§ 2928. Statutory regulations and conditions—Regulations affecting "persons," etc., as applying to corporations.⁵

§ 2930. Insolvent, dissolved or suspended corporations; want of officers. Want of officers does not affect capacity to sue.⁶

§ 2931. Publicly owned, operated or interested corporations. The right to sue a corporation is not affected by the fact that all its stock is owned by the United States government.⁷ So the United States Shipping Board Emergency Fleet Corpora-

¹ See also § 33, supra.

² *Levin v. Miller*, 185 N. Y. App. Div. 856, 173 N. Y. Supp. 667.

³ *Fritz Schulz Jr. Co. v. Raimes & Co.*, 100 N. Y. Misc. 697, 166 N. Y. Supp. 567, and see § 33, supra.

⁴ *Coliseum Athletic Ass'n v.*

Dillon, — Mo. App. —, 223 S. W. 955.

⁵ See § 54, supra.

⁶ *Jones Min. Co. v. Cardiff Mining & Milling Co.*, — Utah —, 191 Pac. 426, quoting *Fletcher Cyc. Corp.* § 2930:

⁷ *Lord & Burnham Co. v. United*

tion, a private corporation, was subject to suit, although the stock was nearly all held by the United States.⁸ But the state cannot be sued for services rendered a hospital although it is a state institution supported by the state, where it is a corporation which can itself be sued.⁹

§ 2936. Equitable actions in general. So far as coming into court with clean hands is concerned, a corporation is not answerable for acts of a stockholder disconnected with the action of the corporation.¹⁰ A contract will not be specifically enforced in favor of a common carrier company merely because of the nature of the company.¹¹ Specific performance by a corporation of an agreement to issue mortgage bonds will not be granted where the agreement is uncertain, or merely as to the portion of the agreement favorable to plaintiff.¹² Specific performance of a contract to assign certain contracts to a corporation cannot be compelled until the corporation is created and comes into existence.¹³

Where timber land is sold by a corporation prior to certain trespasses, the purchaser may sue in equity to recover the value of the timber cut although the sale was consummated subsequent to the trespass.¹⁴

§ 2940. Tort actions; case, trespass, replevin, ejectment, etc. A corporation may sue for libel reflecting on the management of its trade or business;¹⁵ but "written or printed words, to be libelous per se of a corporation, must injuriously and directly

States Shipping Board Emergency Fleet Corporation, 265 Fed. 955; Panama R. Co. v. Curran, 256 Fed. 768.

⁸ Commonwealth Finance Corporation v. Landis, 261 Fed. 440.

⁹ Watkins Boating Co. v. State, 106 N. Y. Misc. 693, 175 N. Y. Supp. 310.

¹⁰ Council of Defense v. International Magazine Co., 267 Fed. 390, and see § 22 et seq., supra.

¹¹ Consolidated Fuel Co. v. St. Louis S. R. Co., 250 Fed. 395.

¹² Beal v. United Properties

Co. of California, — Cal. App. —, 189 Pac. 346. See also Smith v. Central & Pacific Improvement Corporation, — Cal. App. —, 187 Pac. 456.

¹³ Meyer v. Kauffmann, 105 N. Y. Misc. 512, 173 N. Y. Supp. 601, and see § 404, supra.

¹⁴ Baker-Matthews Mfg. Co. v. Grayling Lumber Co., 134 Ark. 351, 203 S. W. 1021.

¹⁵ Puget Sound Nav. Co. v. Carter, 233 Fed. 832; Coal Land Development Co. v. Chidester, — W. Va. —, 103 S. E. 923.

affect its credit or property, and necessarily and directly occasion it pecuniary injury.”¹⁶ A corporation may sue for libel without proof of special damage where the charge directly affects the credit or management of the business and necessarily causes pecuniary loss.¹⁷

A corporation may be sued for maintenance in assisting others to enforce legal rights.¹⁸

§ 2945. Ancillary remedies and proceedings; discovery, injunction, receivers, etc.¹⁹ Where there is no allegation in a petition by a stockholder that he has been denied access to the company's books, or that he is in ignorance of any fact disclosed thereby, or that they do not truthfully exhibit the company's affairs and condition, a judgment for disclosure of the financial condition of the company is not warranted.²⁰

§ 2946. Intervention and interpleader. A corporation may bring an interpleader suit where stock of a deceased person is claimed by two or more, and in such a case costs and solicitor's fees may be allowed it.²¹ Federal statutes give federal courts jurisdiction of suits of interpleader by insurance companies in certain cases.²²

§ 2949. Conditions precedent to actions. The right of a corporation to sue is not barred by failure to make an annual report or pay a franchise tax, as required by statute, where such failure is made by such statute ground for an action to annul the charter but no such action has been brought.²³ The California statute providing that corporations which fail to file

¹⁶ *Vitagraph Co. v. Ford*, 241 Fed. 681.

¹⁷ *First Nat. Bank of Waverly v. Winters*, 225 N. Y. 47, 121 N. E. 459, rev'g 174 N. Y. App. Div. 898, 159 N. Y. Supp. 923, where a bank was charged with violating the excise law to protect its securities and burning a building to obtain insurance.

¹⁸ *Neville v. London Express Newspapers, Ltd.*, [1917] 1 K. B. 402.

¹⁹ Scope of interrogatories to corporate officers, in federal courts, see *Union Sulphur Co. v. Freeport Texas Co.*, 234 Fed. 194.

²⁰ *Bickel v. Henry Bickel Co.*, 184 Ky. 582, 212 S. W. 602.

²¹ *Thomas Kay Woolen Mill Co. v. Sprague*, 259 Fed. 338.

²² *Penn Mut. Life Ins. Co. v. Henderson*, 244 Fed. 877.

²³ *Jones v. Bank of Commerce of Ft. Smith*, 131 Ark. 362, 199 S. W. 103.

a copy of their articles of incorporation in counties where property held by them is located "cannot maintain or defend any action or proceeding relating to such property * * * until such articles of incorporation * * * are filed" is complied with by a defendant who files a certified copy before he files his answer but not until after the filing of the complaint.²⁴

§ 2951. Limitations of actions; laches and estoppel.²⁵ In some states, the constitution expressly provides that no different period of limitations shall be prescribed in actions against corporations than those applicable to actions against natural persons.²⁶ Special statutes of limitation sometimes apply to particular corporations, and have been construed as changing the general statute making infancy of the person injured lengthen the period of limitation.²⁷ A contract made in Florida by agents in charge of the Florida department of a Minnesota corporation is a Florida contract governed by the Florida statute of limitations, where there were no restrictions on the authority of the Florida agents.²⁸ Payment by one company does not toll limitations as to another even though they are joint debtors or the one a surety for the other.²⁹

Laches of a corporation in suing cannot be excused because of lack of officers or cessation of business.³⁰ So loss of corporate books does not excuse laches in suing, where there is no showing as to efforts to find the books.³¹

§ 2952. Defenses by or against corporation—In general. Unlawfully changing the principal place of corporate business without complying with statutory requirements does not authorize the breach of a contract with the corporation.³²

²⁴ *McCann v. Children's Home Society*, 176 Cal. 359, 168 Pac. 355, and see § 215 et seq., supra.

²⁵ Effect of appointment of receiver, see § 5345, *infra*.

²⁶ See *Com. v. Dollar Sav. Bank*, 259 Pa. 138, 1 A. L. R. 1048, 102 Atl. 569.

²⁷ *Grabert v. Central R. Co. of New Jersey*, 91 N. J. L. 604, 103 Atl. 212.

²⁸ *Kamper v. Hunter Land Co.*, — Minn. —, 178 N. W. 747.

²⁹ *White v. Pittsburgh Vein Coal Co.*, — Pa. —, 109 Atl. 873.

³⁰ *Jones Min. Co. v. Cardiff Mining & Milling Co.*, — Utah —, 191 Pac. 426.

³¹ *Jones Min. Co. v. Cardiff Mining & Milling Co.*, — Utah —, 191 Pac. 426.

³² *Kern Horse Remedy Co. v. Selner*, 172 N. Y. App. Div. 152, 158 N. Y. Supp. 192.

§ 2953. — **Statutory provisions; usury, etc.** In New York, by statute, usury cannot be set up as a defense by corporations.³³ Statutes forbidding usury as a defense to corporations are sometimes construed as not applicable to ordinary corporate debts.³⁴ Such statutes do not prevent a debtor corporation from insisting that only interest at the legal rate shall be allowed in determining the amount due the creditor.³⁵ Where a corporation cannot, by statute, plead usury as a defense, a stockholder owning nearly all the stock and who guaranteed the debt cannot set up usury.³⁶ State statutes as to usury do not apply to national banks.³⁷

A corporation cannot avail itself of usury as to old dissolved companies whose successor it is.³⁸

Failure to pay an annual license fee, as barring an action by the corporation, is waived as a defense where not specifically urged on the trial.³⁹

§ 2954. **Abatement and revival—In general.** Actions to recover damages for fraud in sale of stock do not survive the death of the tort-feasor, in some states.⁴⁰

§ 2955. — **Effect of insolvency, bankruptcy, receivership or dissolution.**⁴¹

³³ *Buchholz v. Granite Sav. Bank & Trust Co.*, 261 Fed. 75; *Salvin v. Myles Realty Co.*, 227 N. Y. 51, 6 A. L. R. 581, 124 N. E. 94, holding defense could not be interposed by holder of substantially all the stock; *Scheidell v. Llewellyn Realty Co.*, — N. Y. Misc. —, 177 N. Y. Supp. 529.

³⁴ *Seacoast Real Estate Co. v. American Timber Co.*, 89 N. J. Eq. 293, 104 Atl. 437.

³⁵ *Dorothy v. Commonwealth Commercial Co.*, 278 Ill. 629, L. R. A. 1917 E 1110, 116 N. E. 143, aff'g 198 Ill. App. 601.

³⁶ *Salvin v. Myles Realty Co.*, 227 N. Y. 51, 6 A. L. R. 581 with note, 124 N. E. 94, rev'g 177 N. Y. App. Div. 886, 163 N. Y. Supp. 1131.

³⁷ *Young v. First Nat. Bank of Covington*, 22 Ga. App. 58, 95 S. E. 381.

Usury in case of national banks, see *Mitchell v. Joplin Nat. Bank*, 200 Mo. App. 243, 204 S. W. 1125.

³⁸ *Sugg v. Smith*, — Tex. Civ. App. —, 205 S. W. 363.

Usury as dependent on corporate identity of two companies, see *Brown v. Crawford*, 252 Fed. 248.

³⁹ *Commercial Bank & Trust Co. v. Wenatchee Park Land Irrigation Co.*, 106 Wash. 181, 179 Pac. 798.

⁴⁰ *State ex rel. Baeder v. Blake*, 107 Wash. 294, 181 Pac. 685.

⁴¹ See § 5613 et seq., *infra*.

II. JURISDICTION AND VENUE OR "PLACE OF TRIAL"

§ 2956. **Jurisdiction and its requisites—In general.** Venue statutes do not confer "jurisdiction" over actions against corporations.⁴² Equity has no jurisdiction to bring a corporation, which otherwise would be without its jurisdiction, within the grasp of its process, so as to subject it to a decree in personam or one affecting its property located in another county.⁴³

§ 2957. — **Domicile and citizenship of corporation.** A corporation, domestic or foreign, is presumed to be composed of citizens of the state which created it, for jurisdictional purposes.⁴⁴

§ 2958. — **Citizenship or residence of other parties.** A resident of Alabama will not be enjoined from suing in Georgia a railroad company, for injuries occurring in Alabama, where the company was created in Georgia where it has its principal place of business.⁴⁵

§ 2959. — **Locus of the subject-matter or cause of action.** A transitory action, such as one for personal injuries, may be brought against a corporation in its home state although plaintiff resides, and the accident took place, in another state.⁴⁶ A domestic corporation may be sued by a nonresident in the state of its domicile on a cause of action arising in another state for the wrongful act of a connecting carrier.⁴⁷ The Massachusetts courts have no jurisdiction of actions between foreign corporations created in one state and having mines in another, to re-

⁴² State ex rel. Western Valve Co. v. John Gill & Sons Co., — Mo. App. —, 220 S. W. 978.

Venue of actions against corporations distinguished from jurisdiction, see Moore v. Norfolk & W. R. Co., 124 Va. 628, 98 S. E. 635.

⁴³ Vandersloot v. Pennsylvania Water & Power Co., 259 Pa. 99, 102 Atl. 422.

⁴⁴ Folkes v. Central of Georgia R. Co., 202 Ala. 376, 80 So. 458.

⁴⁵ Folkes v. Central of Georgia R. Co., 202 Ala. 376, 80 So. 458, holding also that where its principal place of business is in its home state it cannot enjoin such a suit because of the disadvantage resulting from the laws of its home state.

⁴⁶ Folkes v. Central of Georgia R. Co., 202 Ala. 376, 80 So. 458.

⁴⁷ MacGovern & Co. v. Atlantic Coast Line R. Co., — N. C. —, 104 S. E. 534.

cover for money expended in Massachusetts for defendant's proportion of expense of pumping water from its mines where the dispute at bottom is one concerning the title to land.⁴⁸ Maine courts have jurisdiction of a suit between domestic corporations arising out of a conversion of ore in Arizona, where title to land was only incidentally involved.⁴⁹

§ 2960. — Character of the proceeding or relief sought. Corporate stock is property, and an action to determine rights in such stock may be based on constructive service of process on nonresident defendants.⁵⁰

§ 2961. — National banks and other national corporations. The United States Shipping Board Emergency Fleet Corporation, although a private corporation, was a public agency created because of the war, and cannot be sued in a state court.⁵¹

§ 2965. Federal jurisdiction—In general. A corporation is not an agent of the government, so as to give a federal court jurisdiction, where it merely has engaged to sell its output to the government.⁵² Where a corporation has fixed or personal property within the district, the fact that most of its property is in another district does not oust a federal court of jurisdiction of a creditor's suit.⁵³ A corporation cannot be sued in a federal court in a state in which neither party resides although it has a usual place of business there.⁵⁴ A suit by a stockholder to cancel a voting trust is not one "to remove any incumbrance or lien or cloud upon the title to real or personal property within the district," so as to confer jurisdiction on a federal court, where complainant and defendant are both nonresidents of the district.⁵⁵ A state statute cannot enlarge the federal

⁴⁸ Arizona Commercial Min. Co. v. Iron Cap Copper Co., — Mass. —, 128 N. E. 4. Emergency Fleet Corporation, 266 Fed. 747.

⁴⁹ Arizona Commercial Min. Co. v. Iron Cap Copper Co., — Me. —, 110 Atl. 429. ⁵² Pickering Land & Timber Co. v. Wisby, 242 Fed. 993.

⁵⁰ Le Roy Sargent & Co. v. McHarg, — S. D. —, 174 N. W. 742. ⁵³ Primos Chemical Co. v. Fulton Steel Corporation, 255 Fed. 427.

⁵¹ Southern Bridge Co. v. United States Shipping Board Dickey, 266 Fed. 587. ⁵⁴ McNeely v. E. I. Du Pont De Nemours Powder Co., 263 Fed. 252.

jurisdiction in equity so as to give jurisdiction of a suit against stockholders where the remedy at law is adequate.⁵⁶

Federal courts follow state decisions construing state statutes relating to corporations.⁵⁷ General rules of corporate law approved by the Supreme Court of the United States will be applied in the federal courts unless there is "a clear, definite and settled rule to the contrary" in the state court.⁵⁸

§ 2966. — Diversity of citizenship; inhabitancy. Where a railroad company is a citizen of and incorporated in two or more states, an action against it in any one of such states is against a citizen of the state, so far as diversity of citizenship is in issue.⁵⁹ Class suits by stockholders may be brought in a federal court where all the complainants reside in a different state from that where the corporation is domiciled, although some of the stockholders who are not complainants reside in the state where the corporation is domiciled.⁶⁰ The citizenship of directors is immaterial, on a question of diversity of citizenship, where they are sued not individually but as representing the corporation.⁶¹ There is no diversity of citizenship, it seems, where a California stockholder brings a stockholder's suit against a Pennsylvania corporation and its officers who are also citizens of Pennsylvania, since the action is in reality in behalf of the corporation.⁶²

There is no collusion fatal to federal jurisdiction on the ground of diversity of citizenship merely because a company controlling another by stock ownership sues the latter, with its consent, and a city, to enjoin interference with the public utility by the city.⁶³

⁵⁶ *Clinton Mining & Mineral Co. v. Cochran*, 247 Fed. 449, South Dakota statute.

⁵⁷ *Ramsay v. Crevlin*, 254 Fed. 813.

⁵⁸ *Thoms v. Goodman*, 254 Fed. 39, 42.

⁵⁹ *Peterborough R. R. v. Boston & M. R. R.*, 239 Fed. 97.

⁶⁰ *Supreme Tribe of Ben Hur v. Cauble*, 264 Fed. 247.

⁶¹ *Gas Securities Co. v. Antero & Lost Park Reservoir Co.*, 259 Fed. 423.

⁶² *Laughner v. Schell*, 260 Fed. 396.

⁶³ *City of Toledo v. Toledo Railway & Light Co.*, 259 Fed. 450.

Joinder of subsidiary company as defendant, in suit by parent company against a labor union, held not collusive, on question of diversity of citizenship, in *Niles-Bement-Pond Co. v. Iron Molders' Union*, 246 Fed. 851.

§ 2967. — Alignment of parties to ascertain diversity.⁶⁴

Where a corporation is made a defendant but joins in the prayer of the bill, it will be aligned as a complainant for the purpose of determining federal jurisdiction.⁶⁵ In determining diversity of citizenship, the citizenship of a subsidiary corporation joined as a defendant is not to be considered where its interests are identical with those of the parent company suing as plaintiff.⁶⁶ A mortgage trustee, made a defendant in a suit by bondholders because of its refusal to sue, where friendly to the bondholders, must be aligned with plaintiffs in determining diversity of citizenship for the purpose of federal jurisdiction.⁶⁷ Where a federal suit is brought by stockholders to set aside a fraudulent transfer of property by the corporation to its president, and both join in an answer denying fraud, the corporation cannot be aligned with complainants to defeat jurisdiction.⁶⁸

§ 2970. Removal of cause to federal court—In general.⁶⁹

The motive of plaintiff in joining an impecunious employee as co-defendant with a nonresident corporation in a negligence suit is immaterial as affecting the right of the corporation to remove the cause to a federal court, where both defendants are jointly liable.⁷⁰ Joinder is fraudulent only where plaintiff has no cause of action against the resident defendant, and has no reasonable ground for supposing that he has, and joins him merely to evade the jurisdiction of the federal court.⁷¹

§ 2971. — Reality and separableness of controversy. There must be a separable controversy to authorize the removal of

⁶⁴ See generally *Brown v. Denver Omnibus & Cab Co.*, 254 Fed. 560.

⁶⁵ *Lindauer v. Compania Palomas de Terrenos y Ganados, Sociedad Anonimo*, 247 Fed. 428.

⁶⁶ In a suit by a corporation against a subsidiary corporation and local labor unions, where no relief is asked against the corporation defendant, it must be aligned with complainant, so that if it is an indispensable party and a citizen of the same state as its co-defendants, a federal court has no jurisdiction. *Niles-Bement-*

Pond Co. v. Iron Moulders' Union, 254 U. S. 77, 65 L. Ed. —, aff'g 258 Fed. 408.

⁶⁷ *Hamer v. New York Rys. Co.*, 244 U. S. 266, 61 L. Ed. 1125.

⁶⁸ *Cutting v. Woodward*, 255 Fed. 633.

⁶⁹ See *Postal Telegraph-Cable Co. v. Puckett*, — Ga. App. —, 101 S. E. 397; *Morrison v. Hartley*, — N. C. —, 101 S. E. 375.

⁷⁰ *Clark v. American Agricultural Chemical Co.*, — N. C. —, 97 S. E. 705.

⁷¹ *Poorman v. Cleveland, C., C. & St. L. R. Co.*, 255 Fed. 985.

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a cause.⁷² A separable controversy exists where the rights of plaintiff against one corporation is based on an express contract while the rights against the other arise out of other transactions having no common origin.⁷³ There is no separable cause of action against a corporation entitling it to remove the case to the federal court where the action is one for damages for personal injuries against the corporation and the alleged negligent employee, the only negligence alleged being that of the employee.⁷⁴

§ 2972. — Diversity of citizenship. Where both plaintiff and defendant are foreign corporations, the case cannot be removed to a federal court because of diversity of citizenship.⁷⁵

§ 2974. — Federal questions and defenses involved. A receiver of a railroad is an officer of the court within the federal statutes authorizing removal of suits against officers of the court.⁷⁶ A quo warranto proceeding by the state on relation of a city to oust a foreign street railway company from the exercise of its franchise to operate the railway on city streets, because of failure to repair streets, etc., as required by the franchise, is a proceeding by the state and cannot be removed to a federal court because of diverse citizenship.⁷⁷

§ 2977. Acquisition, extent and loss of jurisdiction. The Virginia statute authorizing service by publication on domestic corporations having no person in the county on whom process can be served is not a taking of property without due process of law.⁷⁸

⁷² Webb v. Southern R. Co., 248 Fed. 618.

⁷³ Roberts v. Underwood Typewriter Co., 257 Fed. 583. See also State v. Southern R. Co., 255 Fed. 369.

⁷⁴ Baird v. Larabee Flour Mills Co., — Mo. App. —, 220 S. W. 988.

⁷⁵ Kansas Gas & Electric Co. v. Wichita Natural Gas Co., 266 Fed. 614, following Ex parte Wisner, 203 U. S. 449, 51 L. Ed. 264.

⁷⁶ Matarazzo v. Hustis, 256 Fed. 882.

⁷⁷ State v. Reno Traction Co., 41 Nev. 405, L. R. A. 1918 D 847 with note, 171 Pac. 375.

⁷⁸ A. S. White & Co. v. Jordan, 124 Va. 465, 98 S. E. 24, following Ward Lumber Co. v. Henderson-White Mfg. Co., 107 Va. 626, 17 L. R. A. (N. S.) 324, 59 S. E. 477.

§ 2978. Venue or place for trial; privilege and waiver—In general.⁷⁹ A different venue statute may be made applicable to corporations.⁸⁰ Statutes fixing the venue generally of actions by and against corporations are subject to other statutes fixing the venue for special classes of actions.⁸¹ Venue belongs to the procedure or remedy, and hence a corporation has no vested right in a venue statute.⁸²

The venue of actions against corporations is fixed in California by a provision in the constitution.⁸³ In Missouri, by statute, a corporation cannot be sued except in a county where the cause of action accrued or a county where the corporation has or keeps an office or agent for the transaction of its usual and customary business.⁸⁴

Where a statute authorizes actions against a railroad company for personal injuries to be brought in any county in which its lines run, it may be sued in a county where it operated trains over the line of another.⁸⁵

A federal suit to set aside a transaction whereby one company acquired the property of a competitor, as violating the Sherman and Clayton Acts, must be brought in the district where the defendant is an inhabitant.⁸⁶

A corporation, like an individual, may waive its privilege of changing the place of trial.⁸⁷ Corporations, like natural per-

⁷⁹ See *Jones v. Main Island Creek Coal Co.*, — W. Va. —, 99 S. E. 462.

⁸⁰ *Southern Ry. Co. v. Goggins*, 198 Ala. 642, 73 So. 958.

⁸¹ *Wofford-Fain Co. v. Hampton*, 173 N. C. 686, 92 S. E. 612.

⁸² *Southern Ry. Co. v. Goggins*, 198 Ala. 642, 73 So. 958.

⁸³ *Fitzhugh v. University Realty Co.*, — Cal. App. —, 188 Pac. 1023.

⁸⁴ *Moherstadt v. Harry Newman, Inc., Motor Cars*, — Mo. App. —, 217 S. W. 591; *Darby v. Weber Implement Co.*, — Mo. App. —, 208 S. W. 116. See *Riffe v. Wabash R. Co.*, 200 Mo. App. 397, 207 S. W. 78.

Venue of actions against railroad company, under Missouri statutes, see *State ex rel. Hines v. Calhoun*, — Mo. —, 220 S. W. 6, construing phrase "usual and customary business."

⁸⁵ *St. Louis S. W. R. Co. v. Owings*, 135 Ark. 56, 204 S. W. 1147.

⁸⁶ *Venner v. Pennsylvania Steel Co.*, 250 Fed. 292.

⁸⁷ *Dee v. San Pedro, L. A. & S. L. R. Co.*, 50 Utah 167, 167 Pac. 246.

Waiver of right to change of venue where sued jointly with a resident agent, see *Bruce v. State Serum & Supply Co.*, — Iowa —, 177 N. W. 457.

sons, waive the right to change the venue, by first answering to the merits.⁸⁸

§ 2979. — Residence, chief office or principal place of business. A corporation may be sued in the county where it resides, i.e., the county designated in its articles of incorporation as its location.⁸⁹ However, a corporation may be sued in a county other than the one where it has its principal place of business if no objection is made thereto.⁹⁰ The principal place of business of a corporation is its residence, so far as venue is concerned,⁹¹ it is generally held, although there is authority to the contrary. In New York, it has been held that the rule that railroad corporations are deemed to reside in each of the counties through which their road runs, for purposes of venue, does not apply to other domestic corporations having a principal office as fixed in the certificate of incorporation and branch offices in other counties where they transact a part of their business.⁹²

The common-law limitation of venue to the chief place of business has been abrogated by the Pennsylvania statutes so as to authorize an action in a county where the cause of action arose or where the corporation has property or exercises its corporate franchise.⁹³

Injunction suit against a domestic corporation can be brought, in Georgia, only in the county fixed by its charter as the county of its principal office.⁹⁴

A railroad company created by Congress is entitled to be

⁸⁸ Van Kleeck-Bacon Inv. Co. v. Clark, — Colo. —, 180 Pac. 686.

⁸⁹ St. Charles Sav. Bank v. Thompson & Gray Quarry Co., — Mo. —, 210 S. W. 868.

⁹⁰ Dee v. San Pedro, L. A. & S. L. R. Co., 50 Utah 167, 167 Pac. 246.

⁹¹ State ex rel. Western Accident & Indemnity Co. v. District Court, 55 Mont. 380, 176 Pac. 613.

⁹² General Baking Co. v. Daniell, 181 N. Y. App. Div. 501, 170 N. Y. Supp. 365, rev'g 101 N. Y. Misc. 282, 166 N. Y. Supp. 1070.

In the lower court it was held

that the "residence" of a corporation, within venue statutes, is not confined to the county where it has its principal place of business or where its certificate of incorporation is filed, but includes a county where it owns property and actually transacts a substantial part of its business. General Baking Co. v. Daniell, 101 N. Y. Misc. 282, 166 N. Y. Supp. 1070.

⁹³ De Haas v. Pennsylvania R. Co., 261 Pa. 499, 104 Atl. 733.

⁹⁴ Georgia Land & Live Stock Co. v. Savannah River Lumber Co., — Ga. —, 103 S. E. 167.

sued in a federal court in the district of its residence and cannot, without its consent, be sued in the district of the residence of the complainant.⁹⁵

Permitting personal actions against corporations to be brought in a county other than their principal place of business is not unconstitutional as denying to corporations the statutory right of individuals to be sued in the county where they or some of them reside.⁹⁶ In Missouri, after a thorough and lengthy review of the decisions, it is held that its statute providing that libel suits against corporations may be brought in the county where plaintiff resides or where defendant is located, is unconstitutional as a denial of the equal protection of the laws, since libel suits against individuals can be brought only in the county where defendant resides, or where the plaintiff resides and the defendant may be found.⁹⁷ It will be presumed that defendant corporation resided in the county in which suit was instituted where necessary to uphold the jurisdiction of a court of general jurisdiction.⁹⁸

§ 2980. — Place of injury, or of contract, or of accrual of cause. In Texas, by statute, actions against private corporations may be commenced in any county in which the cause of action, or a part thereof, arose; and the question which ordinarily arises is in what county a particular cause of action, or part thereof, arose.⁹⁹ In Missouri, a corporation may be sued

⁹⁵ *Male v. Atchison, T. & S. F. R. Co.*, 240 U. S. 97, 60 L. Ed. 544.

⁹⁶ *Raphael v. People's Bank of Benicia*, — Cal. App. —, 187 Pac. 53, following *Cook v. W. S. Ray Mfg. Co.*, 159 Cal. 694, 115 Pac. 318.

⁹⁷ *McClung v. Pulitzer Pub. Co.*, 279 Mo. 370, 214 S. W. 193.

⁹⁸ *St. Charles Sav. Bank v. Thompson & Gray Quarry Co.*, — Mo. —, 210 S. W. 868.

⁹⁹ See *Trousdale v. Southern Rice Growers' Ass'n*, — Tex. Civ. App. —, 221 S. W. 322; *C. C. Slaughter Cattle Co. v. Pastrana*, —Tex. Civ. App. —, 217 S. W. 749; *Diamond Mill Co. v. Adams-Childers Co.*, — Tex. Civ. App. —,

217 S. W. 176; *Pittman & Harrison Co. v. Boatenhamer*, — Tex. Civ. App. —, 210 S. W. 972; *Beaumont Cotton Oil Mill Co. v. Hester*, — Tex. Civ. App. —, 210 S. W. 702; *Texas Seed & Floral Co. v. Schnoutze*, — Tex. Civ. App. —, 209 S. W. 495; *Garrett v. J. A. Hughes Grain Co.*, — Tex. Civ. App. —, 208 S. W. 758; *Cummer Mfg. Co. v. Lilly*, — Tex. Civ. App. —, 204 S. W. 1010; *Baker-Hanna & Co. v. Kempner*, — Tex. Civ. App. —, 204 S. W. 350; *Cummer Mfg. Co. v. Kellam Bros.*, — Tex. Civ. App. —, 203 S. W. 463; *Wright v. M. M. Graves Co.*, — Tex. Civ. App. —, 198 S. W. 998.

in the county where the cause of action accrued.¹ In California, an action against a local company on a contract may be brought in the county where the contract is to be performed although not the place of business of the company; and this includes the right to have the action tried in such county.² In Wisconsin, the place where a corporate contract was made and where default in payment occurred governs the place of trial of an action for breach of such contract.³

§ 2981. — Any county in state, or where agency or business is conducted, or railroad or other property is situated. In Alabama it is expressly provided that a corporation may be sued "in any county in which it does business by agent," with a certain exception;⁴ and thereunder, if defendant corporation does not do business in the county where plaintiff resides, the corporation may be sued for a tort in any county in the state where it does business by an agent.⁵ In Arkansas, a statute provides that corporations which maintain a branch office or

In Texas it becomes necessary to determine what is meant by "cause of action" and what is meant by "arose," but it would seem that the decision of these questions is in no wise peculiar to the law of corporations. In a particular case, however, where suit was brought against an insurance company by a general agent for compensation, it was held that the cause of action arose in a county in and around which he was to perform services, where he made his office headquarters, and where he was partly paid for his services. *San Jacinto Life Ins. Co. v. Boyd*, — Tex. Civ. App. —, 214 S. W. 482.

The "cause of action" is made up of the contract and its breach. *Cuero Cotton Oil & Manufacturing Co. v. Feeders' Supply Co.*, — Tex. Civ. App. —, 203 S. W. 79.

In Texas, an action for breach of a contract by a corporation

may be brought in the county where the contract was made. *Dallas Waste Mills v. Early-Foster Co.*, — Tex. Civ. App. —, 218 S. W. 515.

¹ *St. Charles Sav. Bank v. Thompson & Gray Quarry Co.*, — Mo. —, 210 S. W. 868.

The cause of action on a life insurance policy, for the purpose of determining venue, accrues at the place where the insured dies. *Roberts v. American Nat. Assur. Co.*, 201 Mo. App. 239, 212 S. W. 390.

² *Raphael v. People's Bank of Benicia*, — Cal. App. —, 187 Pac. 53.

³ *State ex rel. News Pub. Co. v. Park*, 166 Wis. 386, 165 N. W. 289.

⁴ *Tennessee Coal, Iron & Railroad Co. v. Bunn*, 202 Ala. 700, 79 So. 360.

⁵ *Atlantic Coast Line R. Co. v. Ballard*, 202 Ala. 354, 80 So. 436.

other place of business in any county may be sued in such county by serving the agent or employee in charge.⁶ In South Carolina, by statute, corporations may be sued in a county where an agent is maintained for the purpose of transacting corporate business.⁷ In Washington, by statute, actions against corporations may be brought in any county where it is transacting business.⁸ A corporation does not transact business in a county, so as to be suable therein within the Washington statute, because of casual or occasional transactions therein not a part of its ordinary business.⁹

§ 2982. — **Local actions.** An action relating to shares of stock does not involve real property, within venue statutes.¹⁰

§ 2983. **Change of venue or place of trial; transfer of cause — In general.** "A corporation clearly has the same right to a change of venue on account of the prejudice of the trial judge as is accorded to any other litigant."¹¹ In New York, under a 1911 amendment, where an action is brought against a corporation in a county other than its principal place of business, plaintiff may defeat a motion for a change of venue by showing convenience of witnesses.¹²

§ 2984. — **Application and procedure.** Conceding that an affidavit for a change of venue must be made by the party and not by his agent or attorney, an affidavit on behalf of a corporation may be made by an executive or administrative officer of the corporation, such as the president, vice president, secretary or treasurer, but not by an agent or attorney; and the general or managing agent within the state of a corporation of another state is not such an officer as may make the affidavit.¹³

⁶ Rice Belt Tel. Co. v. Malcolm, 131 Ark. 227, 199 S. W. 76, holding statute not repealed by 1913 statutes.

⁷ Fair v. Dorchester Lumber Co., — S. C. —, 101 S. E. 845.

⁸ Cohagen v. Big Ben Land Co., — Wash. —, 186 Pac. 1070.

⁹ State v. Superior Court, — Wash. —, 193 Pac. 229.

¹⁰ Page v. Walser, 43 Nev. 422, 187 Pac. 509.

¹¹ Fidelity & Casualty Co. of New York v. Carroll, 186 Ind. 633, 117 N. E. 858.

¹² Behrman v. Pioneer Pearl Button Co., 190 N. Y. App. Div. 843, 181 N. Y. Supp. 59.

¹³ Fidelity & Casualty Co. of New York v. Carroll, 186 Ind. 633, 117 N. E. 858.

III. PROCESS, SERVICE AND APPEARANCE

§ 2986. Form and sufficiency of original process—Direction and command of writ; name and description. Jurisdiction over a corporation cannot be obtained by a summons directed against and served on a corporate officer. It must be “directed” against the corporation.¹⁴ A judgment by default against a corporation is not voidable because the word “River” in its corporate name was omitted from the summons, where the name was correctly stated in the copy of the complaint served and in the officer’s return.¹⁵

§ 2988. Service of process—In general. The Missouri statutes relating to service of process on corporations apply to justice courts.¹⁶ In some states, equity rules provide that service of the bill and notice to appear and answer, on a corporation, shall be effected in the mode prescribed by law for the service of a writ of summons upon such corporation.¹⁷

§ 2989. — Necessity of strict procedure. In Oklahoma, the statutory method of serving process on corporations is exclusive and must be followed.¹⁸

§ 2990. — In federal courts. State statutes as to how process may be served on a railroad corporation do not govern in a proceeding in personam in equity to which the federal Conformity Act does not apply.¹⁹

§ 2991. Person to be served—In general. Who may be served with process depends on the terms of the governing statute in most states.²⁰ The person to be served depends, under the

¹⁴ Kentucky Bonding Co. v. Com., 178 Ky. 605, 199 S. W. 807.

¹⁵ Tennessee River Nav. Co. v. Hodges, 202 Ala. 15, 79 So. 300.

¹⁶ Burrell Collins Brokerage Co. v. New York Cent. R. Co., — Mo. App. —, 219 S. W. 105.

¹⁷ Vandersloot v. Pennsylvania Water & Power Co., 259 Pa. 99, 102 Atl. 422.

¹⁸ Shawnee Tecumseh Traction Co. v. Webster, — Okla. —, 174 Pac. 266; Cleveland County v. Oklahoma Sanitarium Co., — Okla. —, 165 Pac. 171.

¹⁹ Norfolk Southern R. Co. v. Foreman, 244 Fed. 353.

²⁰ Morris v. Cumberland Producing & Refining Co., 187 Ky. 15, 218 S. W. 302.

statutes in some of the states, on whether the summons is served in the county where the action is brought or in another county.²¹ Special statutes often expressly provide as to who may be served with process in actions against railroad companies.²² Service on one supposed to be the president of a corporation but who in fact was not such, is the same as no service.²³ Service cannot be made on one who is an agent of a creditor's committee rather than an agent of the corporation.²⁴ Service on a de facto officer cannot be questioned by the corporation.²⁵

Where there is no statute, service of papers on a corporation should ordinarily be made on an executive officer or on some agent whose ordinary duties are such that notice to him would naturally insure knowledge to the corporation.²⁶

Process may be served on a domestic corporation as an agent of a foreign corporation, where in reality an agent although the contract between them provides that the relation of principal and agent should not exist.²⁷

According to admiralty practice, service of citation may be made on the secretary of a corporation in a proceeding in personam.²⁸

Service of papers on one not a proper person to be served is not sufficient merely because they came into the hands of a director who was subject to service.²⁹

An officer of a corporation is privileged from service of process on him as a representative of the corporation, where attending court outside the state, the same as if he was claiming the exemption as an individual.³⁰

²¹ See *Morris v. Cumberland Producing & Refining Co.*, 187 Ky. 15, 218 S. W. 302.

²² *Shawnee Tecumseh Traction Co. v. Webster*, — Okla. —, 174 Pac. 266.

²³ *State of New Jersey v. Shirk*, — Ind. App. —, 127 N. E. 861.

²⁴ *Burger v. St. Louis Bed & Manufacturing Co.*, 206 Ill. App. 256.

²⁵ *G. Elias & Bro. v. Boone Timber Co.*, — W. Va. —, 102 S. E. 488.

²⁶ *Starke v. S. G. Beckwith Special Agency*, 227 N. Y. 42, 124 N. E. 96, rev'g 176 N. Y. App. Div. 910, 162 N. Y. Supp. 1145.

²⁷ *McNeill v. Electric Storage Battery Co.*, 109 S. C. 326, 96 S. E. 134.

²⁸ *Norfolk Southern R. Co. v. Foreman*, 244 Fed. 353.

²⁹ *New York City v. Staten Island Midland Ry. Co.*, — N. Y. Misc. —, 180 N. Y. Supp. 1.

³⁰ *Lonsdale Grain Co. v. Neil*, — Okla. —, 175 Pac. 823.

§ 2993. — **President, chief officer and other officers.** Service may be made on the vice president where the president is temporarily absent.³¹ Service should be made on the president rather than the cashier of a bank, as the person in charge, in the absence of a showing to the contrary.³² In Kentucky, the term "chief officer or agent" is expressly defined as including the president, vice president, secretary or librarian, cashier or treasurer, clerk, or managing agent.³³

§ 2994. — **Managing agent, superintendent, etc., other than executive officers.**³⁴ In New York service can be made on a general manager only if specified officers cannot be found with due diligence.³⁵ A superintendent of a street railway, having charge of the operation of cars and employing motormen and conductors, but who in fact was merely an assistant to the general manager, is not a "managing agent" who may be served with process and notices.³⁶

Under the Oklahoma statute authorizing service on "the president, mayor, chairman of the board of directors, or trustees, or other chief officer" or "if its chief officer is not found in the county, upon its cashier * * * or managing agent," service on the managing agent is sufficient where the president is not found in the county, regardless of whether the vice president can be found in the county.³⁷ In that state, service of summons on the superintendent of a railroad company is not authorized, unless he is in charge of a depot or station.³⁸

§ 2996. — **Local agent or person in charge, or other special agents.** The fact that the person served was an employee of

³¹ Chapman v. North American Life Ins. Co., 212 Ill. App. 389.

³² North Georgia Banking Co. v. Fancher, 23 Ga. App. 683, 99 S. E. 229.

³³ See Kentucky Bonding Co. v. Com., 178 Ky. 605, 199 S. W. 807.

³⁴ The manager of a telegraph office, not an executive officer, as subject to service of process, during government control, see Western U. Tel. Co. v. Laslie, — Ala. App. —, 84 So. 864.

³⁵ Birkenwald v. May Co., 179 N. Y. App. Div. 658, 166 N. Y. Supp. 1073.

³⁶ New York City v. Staten Island Midland Ry. Co., — N. Y. Misc. —, 180 N. Y. Supp. 1.

³⁷ Colonial Refining Co. v. Lathrop, — Okla. —, L. R. A. 1917 F 890, 166 Pac. 747.

³⁸ Shawnee Tecumseh Traction Co. v. Webster, — Okla. —, 174 Pac. 266.

the government because of the federal control of railroads does not prevent his also being an agent of the railroad subject to service of process.³⁹

§ 2998. — Registered agent or designated official to receive service. A corporation, although a domestic one, may empower any citizen of the state to accept, as agent, service of process in actions brought against it.⁴⁰ However, service of process may be made on a domestic corporation in the manner pointed out by statute, although the corporation has specially appointed a person on whom process may be served.⁴¹

A domestic corporation cannot object that the person served as its agent appointed by it, as required by statute, to receive service, had moved out of the county where its principal place of business was located, where it had appointed no one to take his place after his removal, although the statute required the appointee to be a resident of the home county.⁴² A statute requiring the appointment of a resident agent by domestic corporations not doing or carrying on business within the state, and also a designation in the articles of incorporation of the residence of such agent, was intended to locate a place at which such agent can be found for the service of process, and such residence may be either at the place of business of the corporation or at its domiciliary office.⁴³

In Michigan, under the new Judicature Act, if the commissioner of insurance has been appointed by any insurance company as an officer on whom process may be served, service on him is a good service.⁴⁴

§ 3000. — Ordinary agents and employees in general. In Georgia, an agent of a corporation, on whom process may be

³⁹ Vicksburg, S. & P. R. Co. v. Anderson-Tully Co., 261 Fed. 741.

⁴⁰ State v. Le Roy Sargent & Co., — Minn. —, 177 N. W. 633.

⁴¹ State v. Le Roy Sargent & Co., — Minn. —, 177 N. W. 633.

A statute requiring a designated agent to be appointed by a corporation to receive service of process ordinarily does not affect other statutes authorizing serv-

ice on certain officers. Kentucky Bonding Co. v. Com., 178 Ky. 605, 199 S. W. 807.

⁴² G. Elias & Bro. v. Boone Timber Co., — W. Va. —, 102 S. E. 488.

⁴³ State ex rel. Chamberlain v. Public Drug Co., 41 S. D. 287, 170 N. W. 161.

⁴⁴ Drueke-Lynch Co. v. Corson, 204 Mich. 180, 170 N. W. 43.

served, must be an agent as distinguished from a mere subordinate employee or servant, although he need not be in charge of the office and business.⁴⁵

§ 3003. — Dissolution, suspension or dormancy of corporation.⁴⁶ Summons against a railroad company cannot be served on an agent of the receiver.⁴⁷ Where a receiver takes over the property of a railroad, service of summons, in an action against the company, cannot be made on a station agent retained in his employment by the receiver, since the appointment of the receiver in itself destroyed the relation of employer and employee as between the railroad company and the station agent.⁴⁸

§ 3005. Substituted or constructive service—In general. An action to determine rights in stock is one in rem and may be based on constructive service of process on nonresident defendants.⁴⁹ A statute authorizing service by publication on domestic corporations having no one who may be served in the county in which the action is brought does not violate the due process of law provision.⁵⁰ A return that "defendant" cannot be found is sufficient as a basis for service by publication, even where defendant is a corporation and there is no statement that officers or agents could not be found to be served.⁵¹

§ 3006. — Application and procedure.⁵²

§ 3007. Place for service—In general. Service on a station agent at the depot is good, although outside the county, where the depot grounds are partly in the county.⁵³ Process is served

⁴⁵ Georgia Railway & Power Co. v. Head, — Ga. —, 103 S. E. 158, holding particular employee at power plant not an agent within the statute.

⁴⁶ Service of summons in actions against receivers, see § 5348, *infra*.

⁴⁷ Vann v. Missouri, K. & T. R. Co., 103 Kan. 857, 176 Pac. 652.

⁴⁸ Chillette v. Missouri, K. & T. R. Co., 102 Kan. 297, L. R. A. 1918 C 1147, 171 Pac. 14.

⁴⁹ Le Roy Sargent & Co. v. Mc-Haig, — S. D. —, 174 N. W. 742.

⁵⁰ A. S. White & Co. v. Jordan, 124 Va. 465, 98 S. E. 24.

⁵¹ Ad Valorem Min. Co. v. Miller, 274 Mo. 696, 204 S. W. 387.

⁵² Sufficiency of affidavit for publication of summons where plaintiff is a corporation, see Jotter v. Charles B. Marvin Inv. Co., — Colo. —, 189 Pac. 22.

⁵³ St. Louis & S. F. R. Co. v. Mobley, — Okla. —, 174 Pac. 510.

at "other place of business" of a corporation where served on an agent employed to buy milk in a county where it had a building to receive milk, its principal place of business being in another county.⁵⁴ Under the Iowa statute providing that when a corporation has a business office or agency in any county outside its main office, service may be had on any agent or clerk employed in such office or agency, in all actions growing out of or connected with the business of that office or agency, a dealer selling machinery of a certain company is not such an agent although having the exclusive right to sell such machinery in the locality.⁵⁵

§ 3012. Return or proof of service—In general. Return of service must show a compliance with the statute.⁵⁶ It must state the position held by the person served.⁵⁷ When a summons is served on a person who is the chief officer or agent of defendant corporation, the return should state the position he holds so that the court may be advised whether he was a chief officer or agent within the statute describing such officers.⁵⁸ A return of service on a corporation on an agent in charge of "its office" is sufficient although the statute requires service at the "business" office.⁵⁹ A return showing service on a named person, "being then and there an agent of the said corporation in charge of its office in said county" is sufficient to show service on the agent while he was at and in charge of the office.⁶⁰ A return of service of process on a clerk of the court, permitted in case service cannot otherwise be obtained, is defective where it fails to recite the facts showing authority to make the substituted service.⁶¹ A return of service of a notice to take depositions is not fatally defective

⁵⁴ *Terry Dairy Co. v. Parker*, — Ark. —, 223 S. W. 6.

⁵⁵ *Duhigg v. Waterloo Gasoline Engine Co.*, — Iowa —, 178 N. W. 530.

⁵⁶ *Ham v. Louisiana & N. W. R. Co.*, 142 La. 186, 76 So. 604.

⁵⁷ *Morris v. Cumberland Producing & Refining Co.*, 187 Ky. 15, 218 S. W. 302.

⁵⁸ *Morris v. Cumberland Pro-*

ducing & Refining Co., 187 Ky. 15, 218 S. W. 302.

⁵⁹ *Bedell v. Richardson Lubricating Co.*, 201 Mo. App. 251, 211 S. W. 104.

⁶⁰ *Bedell v. Richardson Lubricating Co.*, 201 Mo. App. 251, 211 S. W. 104.

⁶¹ *Builders' Supply Co. of Howell, Inc. v. Piedmont Lumber Co.*, 122 Va. 225, 94 S. E. 938.

because of failure to show the statutory conditions relating to the appointment by domestic corporations of an agent to receive service.⁶²

§ 3013. — Effect and conclusiveness when questioned. The return of service is not conclusive as to whether the person served is the agent of the corporation being sued.⁶³ In some states it is expressly provided that the return of the officer executing the summons that the person to whom delivered is the agent of the corporation shall be prima facie evidence of such fact and authorize judgment by default without further proof of such agency, and that such fact need not be recited in the judgment.⁶⁴ In Missouri, where service of process is made on the president or other chief officer, the return need not recite that the service was had in the business office of the company, and such a recital is surplusage and may be rejected.⁶⁵

A return may be amended where it contains a misdescription of the office held by the person served.⁶⁶

§ 3018. Voluntary appearance.⁶⁷ Where a party is sued as a corporation, it is not in default because it appears by its name without describing itself as a corporation.⁶⁸ There is no appearance of a corporation by a response to a summons on forfeiture of bail where the summons was issued against and served on an officer who made the response himself alone.⁶⁹ A corporation does not enter a general appearance by pleading the statute of limitations and asking for costs.⁷⁰

§ 3019. Waivers and admissions by appearance. Jurisdiction of a federal court of a creditor's suit against a corporation

⁶² *G. Elias Bro. v. Boone Timber Co.*, — W. Va. —, 102 S. E. 488.

⁶³ *State of New Jersey v. Shirk*, — Ind. App. —, 127 N. E. 861.

⁶⁴ *Florida Nursery & Trading Co. v. Watson*, 16 Ala. App. 695, 75 So. 874.

⁶⁵ *St. Charles Sav. Bank v. Thompson & Gray Quarry Co.*, — Mo. —, 210 S. W. 868.

⁶⁶ *Morris v. Cumberland Producing & Refining Co.*, 187 Ky. 15, 218 S. W. 302.

⁶⁷ Appearance as waiving service of process, where corporation afterwards answers and goes to trial, see *Norfolk Southern R. Co. v. Foreman*, 244 Fed. 353.

⁶⁸ *Stewart v. Preston*, — Fla. —, 86 So. 348.

⁶⁹ *Kentucky Bonding Co. v. Com.*, 178 Ky. 605, 199 S. W. 807.

⁷⁰ *Southwestern Surety Ins. Co. v. Walser*, 77 Okla. 240, 188 Pac. 335.

cannot be attacked by creditors on the ground of nonresidence of the corporation, where the corporation has voluntarily appeared.⁷¹

§ 3020. Authority to enter appearance for corporation. Attorneys have no authority to appear for a corporation where authorized so to do only by the secretary and treasurer who own fifty per cent of the stock.⁷²

IV. PARTIES

§ 3021. General law of parties. In an action by or against a corporation, in its corporate name, its members or stockholders are not in any legal sense parties to the action.⁷³

§ 3022. Actions and suits by or in favor of corporation—In general. A corporation cannot sue for breach of a contract between a stockholder and a third person, although a contract to furnish goods to the corporation and although such stockholder acquired all the stock.⁷⁴ Promoters who have already surrendered secret profits to the corporation are not necessary parties in an action by the corporation against the other parties to the fraud.⁷⁵

§ 3026. Actions and suits against corporation—Necessary or proper co-defendants. Stockholders are not necessary or proper parties to an action against a corporation where they are not affected as individuals but only as stockholders.⁷⁶ Minority stockholders are not necessary parties to a suit by a city to restrain discontinuance of service by a public service company.⁷⁷ A corporation which owns a large part of the stock of a land

⁷¹ *Primos Chemical Co. v. Fulton Steel Corporation*, 255 Fed. 427.

⁷² *Voron & Chait v. Benguiat*, 162 N. Y. Supp. 974.

⁷³ *Favorite v. Superior Court of Riverside County*, — Cal. —, 184 Pac. 15, and see § 22 et seq., supra.

⁷⁴ *Smart Set Specialty Clothing Co. v. Franklin Knitting Mills*, 191 N. Y. App. Div. 33, 180 N. Y.

Supp. 821, and see § 22 et seq., supra.

⁷⁵ *North American Coal & Coke Co. v. O'Neal*, 82 W. Va. 186, 95 S. E. 822.

⁷⁶ *Hand v. Allen*, 294 Ill. 35, 128 N. E. 305, action for an accounting; and see § 34, supra.

⁷⁷ *City of Jamestown v. Pennsylvania Gas Co.*, 263 Fed. 437.

company and is in a position to control its action may be joined as a defendant in an action against the land company to determine conflicting water rights.⁷⁸ A corporation is not a necessary party to an action in its capacity as a controlling stockholder in another corporation, where the action merely involves corporate rights and functions.⁷⁹ In a suit to restrain discontinuance of service by a public utility company, a corporation owning a majority of the stock in the public utility and which controls its management is a necessary defendant.⁸⁰

In tort actions, the corporation and the person by whose act the injury was done may be joined as defendants.⁸¹ A corporation sued for a tort cannot object that the action was dismissed as to its co-defendants who were its stockholders.⁸² Ordinarily corporate officers need not be joined as defendants in an action against a corporation for unfair competition.⁸³

§ 3027. Corporation as co-party in actions between others—
In general. In a suit to hold a corporation liable as majority stockholder, in favor of minority stockholders, for property received, the old company is not a necessary or proper party.⁸⁴ Where no corporate right is asserted in a suit by minority stockholders, the corporation is not a necessary party. This is illustrated by an action by minority stockholders against the majority stockholder on the ground that defendant had used its power as majority holder for its own benefit to the detriment of minority stockholders.⁸⁵ The corporation is a necessary party to a suit to enjoin persons from assuming to act as officers and directors of the corporation.⁸⁶ A subsidiary corporation is a necessary party to a suit by the parent foreign corporation to enjoin interference by the striking employees

⁷⁸ Vineyard Land & Stock Co. v. Twin Falls, Oakley Land & Water Co., 245 Fed. 30.

⁷⁹ General Inv. Co. v. Lake Shore & M. S. Ry. Co., 250 Fed. 160, 172, aff'g 226 Fed. 976.

⁸⁰ City of Jamestown v. Pennsylvania Gas Co., 263 Fed. 437.

⁸¹ Cotton v. Fisheries Product Co., 177 N. C. 56, 97 S. E. 712.

⁸² Peluso v. City Taxi Co., — Cal. App. —, 182 Pac. 808.

⁸³ Wm. A. Rogers, Ltd. v. H. O. Rogers Silver Co., 237 Fed. 887.

⁸⁴ Southern Pac. Co. v. Bogert, 250 U. S. 483, 63 L. Ed. 1099, modifying 244 Fed. 61.

⁸⁵ Bogert v. Southern Pac. R. Co., 244 Fed. 61, aff'g 226 Fed. 500.

⁸⁶ Lindauer v. Compania Palomas de Terrenos y Ganados, Sociedad Anonimo, 247 Fed. 428.

of the subsidiary company which had contracts with plaintiff, performance of which was prevented by the strikers.⁸⁷

§ 3035. Effect of receivership, dissolution, suspension or succession. A corporation which has conveyed all its property may still sue in its own name, where such right is expressly reserved in the conveyance, and need not join its stockholders.⁸⁸

§ 3036. New and additional parties and amendments of parties. The substitution of an individual for a corporate defendant is the substitution of one cause of action for another.⁸⁹ When a corporation is sued and service made on the supposed president, the petition may be amended by substituting the sole owner of the business "doing business as" such corporation as defendant, and serving process on him.⁹⁰

§ 3037. Intervening and interpleaded parties. Stockholders should be permitted to intervene to set aside a default judgment against the corporation, where the judgment appears unjust and excessive.⁹¹

V. PLEADINGS

§ 3041. Naming and describing corporation. Omitting the prefix "The" in pleading a corporate name is immaterial.⁹² Where the name of plaintiff is such as to indicate that it is either that of a partnership or corporation ("The Bremen Foundry & Machinery Works"), a special demurrer lies to the complaint where it does not state whether it is one or the other; but if no objection is made and judgment is entered for the corporation, the judgment is neither void nor voidable since the defect could have been cured by amendment.⁹³ While a cor-

⁸⁷ Niles-Bement-Pond Co. v. Iron Moulders' Union, 254 U. S. 77, 65 L. Ed. —, aff'g 258 Fed. 408.

⁸⁸ Watson-Loy Coal Co. v. Monroe Coal Min. Co., — W. Va. —, 102 S. E. 485.

⁸⁹ Anderson v. Doran, — Mo. App. —, 211 S. W. 80.

⁹⁰ Bush v. Serat, — Mo. App. —, 217 S. W. 865.

⁹¹ Schwabe v. American Rural Credits Ass'n, — Neb. —, 175 N. W. 673.

⁹² Culver v. Philadelphia, B. & W. R. Co., — Del. —, 102 Atl. 980.

⁹³ Bremen Foundry & Machine Works v. Boswell, 22 Ga. App. 434, 96 S. E. 182.

poration may do business under an assumed or false name and be sued by such name, yet in order to apply this doctrine incorporation by some name must be established.⁹⁴

§ 3042. Pleading formation and existence of corporation; necessity—In general. It is not always necessary, where plaintiff is a corporation, to allege corporate existence.⁹⁵ Where an action is brought on a written instrument, payable to "M. Schulz Company," in the name of the company, it is not necessary to allege that plaintiff is a corporation, under the statute providing that actions on written instruments may be brought by parties thereto by the same name by which they are designated in such instrument.⁹⁶

§ 3043. — Mode and sufficiency. An allegation that plaintiff was incorporated on a certain date is held insufficient to show that there was a corporation some four years afterwards, where there is no allegation that it continued to be a corporation.⁹⁷ Alleging defendant is a "mutual chartered company doing business in the state" is a sufficient allegation of corporate existence, as against a demurrer.⁹⁸ A complaint which has attached to and made a part of it a copy of the bond sued on which shows that the surety was a corporation cannot be attacked for failure to allege that the surety is a corporation.⁹⁹ Alleging that a company is a "pretended" corporation is insufficient as a conclusion, without stating the facts.¹

An indictment for larceny, in alleging ownership of the goods by a company, must state its corporate character.² An information sufficiently avers corporate capacity by alleging that the forged check was drawn on a named bank, "a banking corporation organized and existing according to law."³

⁹⁴ *Simpson v. Grand International Brotherhood*, 83 W. Va. 355, 98 S. E. 580.

⁹⁵ *M. Schulz Co. v. Griffith*, 182 Iowa 650, 166 N. W. 101.

⁹⁶ *M. Schulz Co. v. Griffith*, 182 Iowa 650, 166 N. W. 101.

⁹⁷ *Consolidated Concessions Co. v. McConnell*, — Cal. App. —, 180 Pac. 842.

⁹⁸ *United Mut. Fire Ins. Co. v.*

Talley, — Tex. Civ. App. —, 211 S. W. 653.

⁹⁹ *Sogn v. Koetzle*, 38 S. D. 99, 160 N. W. 520.

¹ *Central Bank of West Lebanon v. Martin*, — Ind. App. —, 121 N. E. 57.

² *People v. Picard*, 284 Ill. 588, 120 N. E. 546.

³ *State v. Stegner*, 276 Mo. 427, 207 S. W. 826.

§ 3045. **Pleading change of name or succession.**⁴ A corporation which made a contract under its old name may sue on it in its new name by merely alleging that it was entered into by its former corporate name.⁵

§ 3046. **Pleading authority or warrant to sue or defend.** The complaint need not allege that the corporation prosecutes its action by attorney.⁶

§ 3047. **Pleading in derivative action by stockholder or receiver, etc.** The receiver should allege not only his appointment but also state the facts showing his authority to sue.⁷

§ 3052. **Pleading substance of actionable right—Charter and by-law provisions entering into right of action.** Where a by-law is pleaded, it is not an abuse of discretion to require its substance and date of adoption to be set forth.⁸

§ 3054. — **Corporate power or want of power.** Alleging that a corporation had no power to assign a note is bad as a conclusion of law.⁹

§ 3055. — **Manner and means of corporate action or knowledge; meetings, resolutions or agents.** It is sufficient to allege that an act was done by the corporation and prove that it was done by constituted authority.¹⁰ In an action against a corporation on orders for the payment of money, accepted by defendant, it is sufficient to allege that the corporation accepted the orders without alleging that the acceptance was done by or through the authorized agents of the corporation.¹¹

⁴ Effect of change of name on right to sue and to be sued, see § 747, *supra*.

⁵ *W. T. Rawleigh Co. v. Grigg*, — Mo. App. —, 191 S. W. 1019.

⁶ *Miller v. Berne Hardware Co.*, 64 Ind. App. 473, 116 N. E. 54.

⁷ *Cahall v. Lofland*, — Del. Ch. —, 108 Atl. 752.

⁸ *Baer v. Waseca Milling Co.*, 143 Minn. 483, 173 N. W. 401.

⁹ *Central Bank of West Lebanon v. Martin*, — Ind. App. —, 121 N. E. 57.

¹⁰ *Grand Rapids & I. Ry. Co. v. Jaqua*, — Ind. App. —, 115 N. E. 73.

¹¹ *Firestone Tire & Rubber Co. v. C. E. Herrick*, 34 Cal. App. 675, 168 Pac. 578.

§ 3057. — Officer's or agent's character and authority, or rights and liabilities. In an action on a draft executed solely by an agent of a corporation, where it is sought to hold the corporation liable, the complaint must show that the draft was executed on behalf of the corporation and that the agent possessed authority to execute it.¹² In Connecticut, under the Reformed Procedure, a complaint against both a corporation and its agent, where relief is sought in the alternative because plaintiff does not know which of the two defendants is liable, need not allege that the agent was authorized to act for the corporation.¹³

§ 3059. — Particular causes of action. A corporation may sue for libel without setting out special damage where the words are libelous per se.¹⁴

§ 3062. Joining and separating causes of action—In general.¹⁵ If two causes of action are stated, one against the corporation and one against an officer, they must be separately stated.¹⁶ A cause of action against a corporation for services and money paid may be joined with a cause of action against the stockholders for their proportionate shares under their statutory liability.¹⁷ Separate causes of action against individuals and a corporation cannot be joined.¹⁸

§ 3066. Defensive and dilatory pleadings—Proper method of objection or defense; by whom made. A third person not a party to the action cannot move to dismiss on the ground that defendant company was not a corporation.¹⁹ If an affidavit of

¹² *Thomas v. Newmark Grain Co.*, — Cal. App. —, 181 Pac. 72.

¹³ *E. B. Eames & Co. v. Mayo*, — Conn. —, 106 Atl. 825.

¹⁴ *Den Norske Ameriekalinje Actieselskabet v. Sun Prtg. & Pub. Ass'n*, 226 N. Y. 1, 122 N. E. 463.

¹⁵ See also § 2715, *supra*.

Misjoinder of causes of action, see *Marsch v. Southern New England R. Corporation*, 230 Mass. 483, 120 N. E. 120.

Splitting cause of action based

on one contract, see *Beltz v. Great Western Lead Mfg. Co.*, 251 Fed. 696.

¹⁶ *Orvis v. Howe*, 183 N. Y. App. Div. 1, 170 N. Y. Supp. 264.

¹⁷ *Avery v. Chucawalla Development Co.*, 175 Cal. 644, 166 Pac. 1002.

¹⁸ *Beveridge v. Crawford Cotton Mills*, 257 Fed. 832.

¹⁹ *Dudley v. Carter Red Ash Collieries Co.*, 125 Va. 701, 100 S. E. 466.

defense is made by a corporate agent who is not a regular officer, it must show why it was not made by an officer and aver that affiant has personal knowledge of the facts stated.²⁰

§ 3069. — Objections in abatement and to the jurisdiction.

Where want of jurisdiction is set up by a corporation, facts must be pleaded to show such want of jurisdiction where not apparent on the face of the complaint.²¹

§ 3072. Mode and sufficiency of answers, denials and pleas—Pleading misnomer. Misnomer must be pleaded in abatement, under the common-law procedure.²² Where a corporation is sued by its former name, it may waive the right to plead misnomer and may appear and plead in its true name, with appropriate averments to show that it is the identical party sued.²³

§ 3073. — Pleading nonexistence or nul tiel corporation.²⁴ A plea of nul tiel corporation is a good plea in bar,²⁵ but it must be verified, under the Alabama statute.²⁶ Corporate existence of plaintiff cannot be denied by defendant unless want of corporate existence is pleaded.²⁷ In order for a corporate defendant to deny incorporation, under the Virginia statute, there must be an affidavit denying such incorporation.²⁸

Denial of corporate existence on information and belief is insufficient.²⁹ A denial on information and belief of an allegation that plaintiff was a corporation engaged in insuring property does not put in issue corporate capacity.³⁰

²⁰ *Mintz v. Tri-County Natural Gas Co.*, 259 Pa. 477, 103 Atl. 285.

²¹ *Atlantic Coast Line R. Co. v. Ballard*, — Fla. —, 80 So. 436.

²² *Elbert v. Wilmington Turngemeinde*, — Del. —, 107 Atl. 215.

²³ *Stewart v. Preston*, — Fla. —, 86 So. 348.

²⁴ General denial as sufficient to raise question of corporate existence, see § 3085, *infra*.

²⁵ *Ashurst v. Arnold-Henegar-Doyle Co.*, 201 Ala. 480, 78 So. 386.

²⁶ *Ashurst v. Arnold-Henegar-Doyle Co.*, 201 Ala. 480, 78 So. 386.

²⁷ *Ayash v. Wm. Gerbst Brewing Co.*, — Ga. App. —, 94 S. E. 282.

²⁸ *Dudley v. Carter Red Ash Collieries Co.*, 125 Va. 701, 100 S. E. 466.

²⁹ *Rogers Bros. Co. v. Beck*, — Cal. App. —, 184 Pac. 515.

³⁰ *Westchester Fire Ins. Co. v. Bollin*, 106 S. C. 45, 90 S. E. 327.

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§ 3078. — **Pleading particular defenses of substance.** Ratification need not be specially pleaded.³¹ The illegality of a corporate contract for permanent employment, forbidden by statute, need not be pleaded in order to be invoked as a defense by the corporation in an action against it on such contract.³² Ultra vires must be pleaded.³³

§ 3080. **Amendments and supplemental pleadings.** Allowance of an amendment by denying incorporation of plaintiff is discretionary.³⁴ Misnomer of the corporation is generally amendable,³⁵ but not where defendant corporation does not appear and it is not shown that the right party had been served although by the wrong name.³⁶ If a corporation named as defendant is in court but the complaint incorrectly states where it was incorporated, an amendment is proper to correct the mistake.³⁷ An amendment of the complaint by striking out an allegation that plaintiff, a corporation, entered into the contract sued on, and substituting an allegation that the contract was a partnership one and that the plaintiff corporation became the owner of all the partnership assets, does not change the cause of action and is permissible.³⁸ Where a motion in arrest of judgment is based upon the failure to implead a Nebraska corporation, plaintiff has a right to obviate the fault on which the motion is based by filing an amendment changing an allegation that defendant is a Michigan corporation to one that it is a Nebraska corporation.³⁹ However, service on the secretary of a domestic corporation does not authorize an amendment of the declaration by substituting the name of a Canadian corporation as defendant, where the secretary was not an official of the Canadian corporation.⁴⁰

³¹ Buckeye Cotton Oil Co. v. Sloan, 250 Fed. 712, 725.

³² Williams v. Great Northern R. Co., 108 Wash. 344, 184 Pac. 340.

³³ Coliseum Athletic Ass'n v. Dillon, — Mo. App. —, 223 S. W. 955.

³⁴ Licensed Retail Liquor Dealers' Ass'n v. Denton, 144 Minn. 81, 174 N. W. 526.

³⁵ Denver & R. G. R. Co. v.

Nunez, — Colo. —, 180 Pac. 78, and see §§ 742, 743, supra.

³⁶ Mahan v. Wyopo Co., — Wyo. —, 189 Pac. 633.

³⁷ Bishop-Babcock-Becker Co. v. Hyde, 61 Okla. 250, 161 Pac. 172.

³⁸ Old & Wallace v. Joseph R. Marquette, Jr., Inc., 183 N. Y. App. Div. 583, 170 N. Y. Supp. 84.

³⁹ Boyd v. Buick Automobile Co., 182 Iowa 306, 165 N. W. 908.

⁴⁰ Parke, Davis & Co. v. Grand

§ 3082. **Set-off and counterclaim.** In an action against a national bank in a state court, the practice and pleadings prescribed by the state in regard to a counterclaim or recoupment cannot be resorted to, so as to defeat the object and intent of a federal enactment.⁴¹ A foreign corporation, doing business in Georgia through agents located there, is not a nonresident corporation, within the rule as to pleading recoupment in a tort action.⁴²

§ 3083. **Signature, seal and verifications or affidavits.**⁴³ In Delaware, it is held that an answer in equity must be under the corporate seal;⁴⁴ and in that state the equity rule of court requiring that where there are interrogatories all answers must be under oath, does not apply to a corporation defendant.⁴⁵ The verification of a pleading need not state why the verification is not made by the party nor the grounds of belief, where nothing is alleged on information.⁴⁶ Where a corporation is a domestic one, a verification of a pleading by the president need not set forth the grounds of the affiant's belief as to matters alleged upon information.⁴⁷

§ 3085. **Issues, variance and admissions—Misnomer or misdescription.** A variance as to the state in which plaintiff was incorporated ordinarily is not fatal.⁴⁸

Trunk R. System, 207 Mich. 388, 174 N. W. 145.

⁴¹ *Planters' Nat. Bank of Virginia v. Wyson & Miles Co.*, 177 N. C. 380, 99 S. E. 199, referring to usury statutes.

⁴² *Youngblood v. Armour Fertilizer Works*, 23 Ga. App. 731, 99 S. E. 314.

⁴³ See also § 3073, *supra*.

Verification of pleadings under New York statutes, see *Davidson v. Penn-Virginia Coal & Coke Co.*, 109 N. Y. Misc. 130, 178 N. Y. Supp. 205.

Verification by corporate officer, see part of note on pp. 58, 59 of 1 A. L. R.

⁴⁴ *Hopper v. Fesler Sales Co.*, — Del. Ch. —, 100 Atl. 791; *Whitmer v. William Whitmer & Sons*, — Del. Ch. —, 98 Atl. 940.

⁴⁵ *Hopper v. Fesler Sales Co.*, — Del. Ch. —, 100 Atl. 791. See also *Whitmer v. William Whitmer & Sons*, — Del. Ch. —, 98 Atl. 940.

⁴⁶ *Treen Motors Corporation v. Van Pelt*, 106 N. Y. Misc. 357, 174 N. Y. Supp. 500.

⁴⁷ *Treen Motors Corporation v. Van Pelt*, 106 N. Y. Misc. 357, 174 N. Y. Supp. 500.

⁴⁸ *Tropical Inv. Co. v. Brown*, — Cal. App. —, 187 Pac. 133.

§ 3086. — **As to existence or charter.** Statutes in most of the states expressly provide that, in actions by or against corporations, it is not necessary to prove the existence of such corporation, unless the defendant, in his answer, expressly avers that the plaintiff, or defendant, as the case may be, is not a corporation.⁴⁹ The New York statute providing that corporate existence need not be proved unless denied under oath does not prevent a corporation from proving under a mere general denial the actual date of incorporation to show that the contract sued on was made before incorporation.⁵⁰ In an action for goods sold, where the complaint alleges that at all times mentioned the defendant was a corporation, which allegation was denied by answer, the issue is not confined to whether defendant was a corporation at the time of the commencement of the action.⁵¹

VI. EVIDENCE AND WITNESSES

§ 3088. **Matters judicially noticeable—In general.** Judicial notice will be taken that two persons cannot alone incorporate.⁵² Judicial notice is not taken of what private corporations are or are not domestic corporations;⁵³ of the volume of business done by a telegraph company at a particular office, or the like;⁵⁴

⁴⁹ *Fruth v. Bolt*, 39 S. D. 371, 164 N. W. 270.

Allegation of incorporation of defendant, where not put in issue, need not be proved. *Burke v. Curtis Aeroplane Motor Co.*, — Ala. —, 85 So. 703.

⁵⁰ *Galdieri v. Arthur Waist Co.*, 98 N. Y. Misc. 612, 163 N. Y. Supp. 154.

⁵¹ *Shelton Tack Co. v. Reliable Metal Box Mfg. Co.*, — N. Y. Misc. —, 177 N. Y. Supp. 163, overruling dictum in *Galdieri & Co. v. Arthur Waist Co.*, 98 N. Y. Misc. 612, 163 N. Y. Supp. 514.

⁵² *Jones Min. Co. v. Cardiff Mining & Milling Co.*, — Utah —, 191 Pac. 426.

⁵³ *Mahan v. Wyopo Co.*, — Wyo. —, 189 Pac. 633.

Judicial notice is not taken of

whether a particular corporation was organized under the local statutes. *Mahan v. Wyopo Co.*, — Wyo. —, 189 Pac. 633.

Judicial notice will not be taken of a statute granting the charter of a railroad nor of amendatory acts changing its name. *Dunley v. Chicago, B. & Q. R. Co.*, 200 Ill. App. 75.

But a federal court in New Hampshire takes judicial notice that the Boston & Maine Railroad is incorporated and doing business in New Hampshire, as well as Massachusetts, and hence a citizen of New Hampshire. *Peterborough R. R. v. Boston & M. R. R.*, 239 Fed. 97.

⁵⁴ *Western U. Tel. Co. v. City of Decatur*, 202 Ala. 593, 81 So. 199.

of the appointment by a foreign corporation of an agent on whom process may be served;⁵⁵ nor of the purposes of a Y. M. C. A. local branch, in order to classify it as a charitable corporation.⁵⁶ So what are the offices, held by officers, of a private corporation, is not the subject of judicial notice.⁵⁷

If the name of a party is manifestly a charitable, educational, commercial, manufacturing or financial one, such as are usual objects of incorporation, and not one common to partnerships or individuals, it should import a corporation, and whether it does or not should as a general rule be left to judicial knowledge.⁵⁸

§ 3089. — General common knowledge. Judicial notice will be taken that this country took over the railroads by act of Congress as a war measure;⁵⁹ of the nature and purposes of fraternal associations;⁶⁰ and, in Missouri, that the "University of Missouri" is a corporation.⁶¹

§ 3090. Presumptions and burden of proof—In general. Bank stock is presumed to be worth at least par.⁶²

§ 3091. — As to corporate existence, formation and powers. By-laws are presumed valid.⁶³

§ 3093. — As to officers and agents and their authority.⁶⁴ There is no presumption that corporate officers had acted as

⁵⁵ Existence of his agency by appointment to receive process as required by statute in case of foreign corporations, in case of service on particular agent, cannot be judicially noticed. *National Surety Co. v. Board Sup'rs Holmes County*, 120 Miss. 565, 83 So. 8.

⁵⁶ *Susman v. Y. M. C. A. of Seattle*, 101 Wash. 487, 172 Pac. 554.

⁵⁷ *Ex parte State*, 201 Ala. 59, 77 So. 353.

⁵⁸ *Stewart v. Preston*, — Fla. —, 86 So. 348.

⁵⁹ *Hines v. Wimbish*, — Ala.

—, 85 So. 765; *McDougal v. Louisville & N. R. Co.*, — Ala. App. —, 85 So. 880; *Kneeland-Bigelow Co. v. Michigan Cent. R. Co.*, 207 Mich. 546, 174 N. W. 605.

⁶⁰ *Brown v. Steckler*, 40 N. D. 113, 1 A. L. R. 753, 168 N. W. 670.

⁶¹ *State v. Long*, 278 Mo. 379, 213 S. W. 436.

⁶² *Scandinavian American Bank v. Westby*, — N. D. —, 172 N. W. 665.

⁶³ *Ex parte Baldwin County Producers' Corporation*, 203 Ala. 345, 83 So. 69.

⁶⁴ Burden of proof to show au-

such prior to a resolution that named persons are the officers of the corporation.⁶⁵ There is no presumption that one an officer of a corporation on a certain date continued to be an officer at a later date.⁶⁶

§ 3094. Admissibility, introduction and sufficiency of evidence. In the absence of proof to the contrary, very slight evidence of incorporation will sustain a finding that a party to a contract is a corporation, although not so described in the contract.⁶⁷ A note, although not executed by the proper corporate officer, is admissible in an action against the corporation for money loaned, as evidence tending to establish the loan.⁶⁸ The rule that in case of words libelous per se no proof of special damage is necessary applies where a corporation is libelled.⁶⁹

§ 3096. Best and secondary rule—Organization, objects, character and by-laws and personnel.⁷⁰ Incorporation may be proved orally.⁷¹

§ 3097. — Corporate acts and resolutions. Corporate records are the best evidence of facts shown thereby.⁷² But while ordinarily the official acts of a corporation should be shown by the minutes or other records kept, yet where no records are kept, oral evidence is admissible in their stead.⁷³

thority of officer to execute, in action on unsealed instrument, see § 1943, *supra*.

Presumption as to power of president to execute note, in action on note, see § 2038, *supra*.

Parol evidence to show authority of officers, see § 1904, *supra*.

⁶⁵ Johnson Bros. Lighterage Co. v. American Union Line, 110 N. Y. Misc. 326, 180 N. Y. Supp. 460.

⁶⁶ Hurley v. Randall, — R. I. —, 111 Atl. 530.

⁶⁷ Simpson v. Grand International Brotherhood, 83 W. Va. 355, 98 S. E. 580.

⁶⁸ Scouton v. Stony Brook Lum-

ber Co., 261 Pa. 241, 7 A. L. R. 1433, 104 Atl. 548.

⁶⁹ Cotton Lumber Co. v. La-Crosse Lumber Co., 200 Mo. App. 7, 204 S. W. 957.

⁷⁰ Parol, and best, evidence to show stock ownership, see § 569, *supra*.

⁷¹ See § 425, *supra*.

⁷² Palmer v. Bratager, 41 S. D. 649, 172 N. W. 507.

⁷³ Fields v. Bullington, 20 Ga. App. 102, 92 S. E. 653.

Where no record is made of a directors' meeting, parol evidence as to acts of the board is admissible. Norma Min. Co. v. Mackay, 241 Fed. 640; Copper King Min.

§ 3098. — **Corporate doings and contracts.** Authority from the board of directors to an executive officer to execute a deed or mortgage may be shown by parol.⁷⁴ To prove employment by a board of directors, a resolution of the directors duly entered in the books need not be shown but it is sufficient to show that the board did in fact authorize the employment.⁷⁵

§ 3100. **Parol evidence rule.** Corporate minutes and records are prima facie evidence of the facts stated therein, but parol evidence is always admissible to explain or supplement them where ambiguous or incomplete.⁷⁶ Thus, the full transaction may be shown by parol where only part of it appears in the minutes of the directors' meeting.⁷⁷ So a president of a corporation who signs a contract as such may nevertheless show by parol a collateral agreement personal to himself.⁷⁸ Likewise, the actual consideration for a transfer of stock may be shown by parol.⁷⁹ Parol evidence is also admissible to show the corporate identity of a charitable corporation to whom a bequest had been made.⁸⁰

A subscription to stock comes within the rule that a written contract cannot be impaired or changed by parol.⁸¹ Thus, a subscription contract cannot be varied by parol evidence of the agent of the corporation to show intent, unless stipulations were omitted by mistake, accident or fraud.⁸² So the written contract

Co. v. Hanson, — Utah —, 176 Pac. 623.

Acts of directors may be shown by parol when it is shown that no record was made thereof or that if one was made it had been lost. Copper King Min. Co. v. Hanson, — Utah —, 176 Pac. 623.

⁷⁴ McCartney v. Clover Valley Land & Stock Co., 232 Fed. 697.

⁷⁵ Ney v. Eastern Iowa Tel. Co., 185 Iowa 610, 171 N. W. 26.

⁷⁶ Shuman v. Main, Beaver & Black Creek Mut. Fire Ins. Co., 265 Pa. 38, 108 Atl. 265.

⁷⁷ Lawrence v. Premier Indemnity Assur. Co., — Cal. —, 182 Pac. 431.

⁷⁸ Continental Trust Co. v.

Johnston, — Colo. —, 188 Pac. 1112.

⁷⁹ Fay v. Corbett, 233 Mass. 403, 124 N. E. 73.

⁸⁰ Sisters of Charity v. Emery, 144 La. 614, 81 So. 99.

⁸¹ Bunn v. Farmers' Warehouse Co., 18 Ga. App. 567, 90 S. E. 78; Boushall v. Stronach, 172 N. C. 273, 90 S. E. 198; Mitchell v. Porter, — Tex. —, 223 S. W. 197; Turner v. Cattleman's Trust Co., — Tex. —, 215 S. W. 831; Burchill v. Hermsmeyer, — Tex. Civ. App. —, 212 S. W. 767, and see §§ 569, 577, 609, supra.

⁸² Turner v. Cattleman's Trust Co., — Tex. —, 215 S. W. 831.

of subscription cannot be varied by parol evidence that part of the subscription was made for another, but it may be shown by parol that others agreed to, and did, pay part of the subscription.⁸³ But if the contract is incomplete and executory, parol evidence is admissible to show when the stock was to be issued and delivered.⁸⁴ So parol evidence is admissible to determine the meaning of the word "securities" as used in a stock subscription contract, where ambiguous.⁸⁵

Minutes of directors' meeting are not a written instrument, not subject to contradiction, but instead, in the absence of an estoppel, it is permissible to show by parol exactly what took place at the meeting.⁸⁶ Corporate records do not preclude the other party to a contract from showing that the transaction is not correctly set forth therein, where the adverse party had no part in making the record and has never assented to it; and this rule applies where a corporation deals with a member.⁸⁷ However, corporate minutes cannot be impeached by parol evidence of directors.⁸⁸

§ 3101. Books and records as documentary evidence. The contents of corporate books, where relevant, are admissible,⁸⁹ provided they are not self-serving declarations.⁹⁰ In any event corporate books more than thirty years old are admissible, on proper proof of identity.⁹¹

Corporate records are not evidence in favor of the company to show its intent.⁹² An entry in the minutes of the corpora-

⁸³ *Vaughan-Robertson Drug Co. v. Grimes-Mills Drug Co.*, 173 N. C. 502, 92 S. E. 376.

⁸⁴ *Zapp v. Spreckels*, — Tex. Civ. App. —, 204 S. W. 786.

⁸⁵ *Mitchell v. Porter*, — Tex. Civ. App. —, 194 S. W. 981.

⁸⁶ *Lawrence v. Premier Indemnity Assur. Co.*, — Cal. —, 182 Pac. 431.

⁸⁷ *Daggett v. St. Paul Tropical Development Co.*, 141 Minn. 51, 169 N. W. 252.

⁸⁸ *Great Western Mfg. Co. v. Porter*, 103 Kan. 84, 172 Pac. 1018.

⁸⁹ *Pearson v. Wallace*, 204 Mich. 643, 170 N. W. 72. See *Purick v. Port Jefferson Elec. Light Co.*, 186 N. Y. App. Div. 214, 174 N. Y. Supp. 285.

⁹⁰ *Royce v. Farmers' Life Ins. Co.*, — Kan. —, 191 Pac. 581.

⁹¹ *Geary St., P. & O. R. Co. v. Campbell*, 39 Cal. App. 496, 179 Pac. 453.

⁹² *Com. v. Clark County Nat. Bank*, 187 Ky. 151, 219 S. W. 175.

tion showing that certain stock had been paid for in full is not conclusive against creditors of the corporation.⁹³ Minutes of stockholders' meeting are, however, sometimes admissible in favor of the corporation, as against a third person who was present at the meeting.⁹⁴ Sham and fictitious entries in corporate books are not evidence of the existence of the facts stated in such entries.⁹⁵

§ 3102. Books and records as dis-serving declarations and admissions. A corporation may be estopped to dispute the accuracy of its minutes.⁹⁶

§ 3103. Authentication of books and records for introduction. The charter, to be admissible in evidence, must be a properly certified copy.⁹⁷

§ 3104. Admissions and declarations by officers, agents and stockholders. Admissions or representations of the president of a corporation are not binding on directors, where the former is not an agent of the latter.⁹⁸ Corporate books are admissible against directors in an action by receivers to recover from them unlawful dividends paid.⁹⁹

§ 3105. Modes of proving particular facts—In general.¹

§ 3106. — Corporate existence, incidents and character. The charter of a corporation is admissible in evidence to show the purposes of the corporation or the nature of its business.² To prove nonexistence of a corporation when a sale was made, its certificate of incorporation of a later date is admissible.³

⁹³ Home Sav. Bank v. Los Angeles City Realty Co., — Cal. —, 171 Pac. 290.

⁹⁴ Dakota Coffee Co. v. Johnson, — N. D. —, 178 N. W. 291.

⁹⁵ Axford v. Western Syndicate Inv. Co., 141 Minn. 412, 170 N. W. 587.

⁹⁶ Great Western Mfg. Co. v. Porter, 103 Kan. 84, 172 Pac. 1018.

⁹⁷ See Landis v. State, 85 Tex. Cr. App. 381, 214 S. W. 827.

⁹⁸ Reno v. Bull, 226 N. Y. 546, 124 N. E. 144.

⁹⁹ Hodde v. Nobbe, — Mo. App. —, 221 S. W. 130.

¹ Proof of subscriptions to stock, see § 569, supra.

² C. C. Slaughter Cattle Co. v. Pastrana, — Tex. Civ. App. —, 217 S. W. 749.

³ Midland Trading Co. v. Hechtkopf, — N. Y. Misc. —, 176 N. Y. Supp. 712.

§ 3108. Witnesses in action where corporation is party—Competency where interest of a decedent is adverse. A statutory rule that no person shall be allowed to testify when the other party to the transaction is dead applies to the death of a corporate representative.⁴ But a party to a corporate contract is competent to testify in relation to a personal transaction between himself and a deceased officer of such corporation.⁵ Where one corporation sues another, an officer of the plaintiff may testify as to declarations made by the president, since deceased, of defendant, at least under the terms of the North Carolina statute.⁶ Evidence as to acts of directors or stockholders as a body is not inadmissible as relating to transactions with a deceased stockholder, although he attended such meeting.⁷ A stockholder who had sold his stock is not "interested in the event," as applied to subsequent dealings with the stock, so as to be precluded from testifying against the representative of a deceased person.⁸

The president of a mercantile corporation is presumptively a stockholder, and a person interested in the event of an action against the corporation, so as to be presumptively incompetent, under the statute, to testify as to a conversation with a deceased person relating to a matter in issue.⁹

§ 3109. Subpoenas and notices to produce or to allow inspection.¹⁰

§ 3110. Discovery, inspection and examination or deposition.¹¹ The right to inspect books of a foreign corporation is not precluded, in New York, by the fact that the books are

⁴ *Bright v. Virginia & Gold Hill Water Co.*, 254 Fed. 175, Nevada statute.

⁵ *Keystone Coal & Coke Co. v. Hall*, 83 W. Va. 287, 98 S. E. 572.

⁶ *Fidelity Bank v. Wysong & Miles Co.*, 177 N. C. 28, 98 S. E. 769.

⁷ *Spivey v. Pugh*, 140 Ark. 296, 215 S. W. 739.

⁸ *Kalman v. Reubel*, 191 N. Y. App. Div. 402, 181 N. Y. Supp. 471.

⁹ *Caldwell Milling & Elevator*

Co. v. L. L. May Co., 141 Minn. 255, 169 N. W. 797.

¹⁰ See § 2805, *supra*.

¹¹ Examination of corporation before trial, under New York statutes, see *Harby S. S. Co. v. Staten Island Shipbuilding Co.*, 189 N. Y. App. Div. 769, 178 N. Y. Supp. 818.

Examination of foreign corporation before trial, under statute, see *Sivelli v. New River Coal Co.*, 184 N. Y. App. Div. 935, 171 N. Y. Supp. 429.

outside the state.¹² A corporation is not privileged from the production of its books and papers, even though they tend to incriminate an officer thereof.¹³ In Texas, the statutory right of a party to take depositions applies to corporations.¹⁴

In New York a corporation not a party to an action cannot be examined before trial;¹⁵ and an order for examination before trial must direct the examination of the corporation as an adverse party rather than the examination of one of its officers.¹⁶ The manager of an important branch of a corporation is a "managing agent thereof" within a statute regulating examination of a party before trial.¹⁷

VII. TRIAL AND ITS INCIDENTS

§ 3112. In general. Actions by a corporation to recover from the same defendant a balance due on subscriptions to stock are properly consolidated.¹⁸ Where the only thing in common between two suits against a corporation is an application for a receivership, and a receiver had been appointed in one of the suits, the suits should not be consolidated.¹⁹

§ 3113. Conduct and control; compromise and discontinuance. In case of a corporation, an affidavit for continuance should be made by the president, treasurer or cashier.²⁰

§ 3114. Judge and jury.²¹ A judge owning stock in a company sued with others to recover oil lands is disqualified to sit, under the federal statutes.²² But a judge who has disposed of his

¹² *Wilson v. Van Dorn Iron Works Co.*, 106 N. Y. Misc. 442, 174 N. Y. Supp. 684.

¹³ *Linn v. United States*, 251 Fed. 476.

¹⁴ *El Paso Elec. Ry. Co. v. Sauerennmann*, — Tex. Civ. App. —, 208 S. W. 237.

¹⁵ *Lasher v. Hart*, — N. Y. Misc. —, 170 N. Y. Supp. 931.

¹⁶ *Educational Films Corporation v. Lincoln & Parker Co.*, 192 N. Y. App. Div. 621, 183 N. Y. Supp. 113.

¹⁷ *Miller v. W. K. Jahn Co.*, 104

N. Y. Misc. 370, 172 N. Y. Supp. 219.

¹⁸ *Columbia-Knickerbocker Trust Co. v. Abbot*, 247 Fed. 833.

¹⁹ *Adler v. Seaman*, 266 Fed. 828.

²⁰ *Voorhees Rubber Co. v. Brunswick-Balke-Collender Co.*, — Del. —, 105 Atl. 786.

²¹ Disqualification of judge of appellate court, as policyholder, etc., see *California State Life Ins. Co. v. Kring*, — Tex. Civ. App. —, 208 S. W. 372.

²² *In re Honolulu Consol. Oil Co.*, 243 Fed. 348.

stock before the bringing of an action by or against the corporation is not disqualified unless it is shown that his statutory liability as a stockholder exists notwithstanding his disposal of the stock.²³ The fact that the wife of the judge is a stockholder in a corporation which is a party to a pending suit does not disqualify the judge, under the California statute disqualifying judges in actions to which he is a party or in which he is interested or where he is related to either party by consanguinity or affinity within the third degree.²⁴

A juror who states he is prejudiced against personal injury actions against corporations, is properly rejected in such an action.²⁵ Relationship within the prohibited degrees to a stockholder disqualifies a juror, in a prosecution of the corporation.²⁶

VIII. JUDGMENT AND ENFORCEMENT; APPEAL AND REVIEW

§ 3119. Defaults and confessions. A default judgment against a corporation is void where it does not appear that proof was made that the person on whom service was made was an officer or agent of the defendant corporation.²⁷ Negligence of the statutory agent of a domestic corporation in not notifying it of the pendency of a suit against it is not excused, so as to authorize the setting aside of a default judgment, because he did not know the address of the company, where it appears in the incorporation papers duly filed.²⁸ Stockholders should be permitted to intervene to set aside a default judgment against the corporation, in a proper case.²⁹

Disqualification of stockholder as judge, see 4 Minn. L. Rev. 301-303.

²³ *Favorite v. Superior Court of Riverside County*, — Cal. —, 184 Pac. 15.

²⁴ *Favorite v. Superior Court of Riverside County*, — Cal. —, 184 Pac. 15.

Note on "Disqualification of judge by relative's ownership of stock in corporation which is party to action or proceeding," see 8 A. L. R. 295.

²⁵ *Vessels v. Kansas City Light & Power Co.*, — Mo. —, 219 S. W. 80.

²⁶ *Fordham v. State*, 148 Ga. 758, 98 S. E. 267.

²⁷ *Baker v. Sparks*, 202 Ala. 653, 81 So. 609.

²⁸ *Lynch v. Arizona Enterprise Min. Co.*, 20 Ariz. 250, 179 Pac. 956, citing *Bradshaw v. Des Moines Ins. Co.*, 154 Iowa 101, 38 L. R. A. (N. S.) 420, 134 N. W. 628, and *Reese Lumber Co. v. Licking Coal & Lumber Co.*, 156 Ky. 723, 161 S. W. 1124.

²⁹ *Schwabe v. American Rural Credits Ass'n*, — Neb. —, 175 N. W. 673.

The court has *prima facie* jurisdiction to enter a judgment by confession against a corporation where a note and warrant of attorney are signed by the corporation by its president, without any showing as to the authority of the president.³⁰

§ 3121. Costs and allowances, and security for costs. Counsel fees should not be allowed a stockholder in an action against his corporation which is not for the benefit of any stockholder except himself, especially when the action is to the disadvantage of the other stockholders.³¹

That plaintiff is a foreign corporation is sometimes a statutory ground for requiring security for costs.³²

§ 3123. Amendment, vacation or other relief from judgment.³³

§ 3124. Conclusiveness and effect; collateral attack. A corporation is not bound by a judgment to which it is not a party,³⁴ unless it is in effect a party and has had its day in court.³⁵ A judgment of dismissal is not binding on a corporation which is only technically a party, where the litigation was not conducted in its behalf.³⁶ A judgment against the president of a corporation is not a judgment against the corporation, and the latter can restrain dispossession of it under such a judgment.³⁷

³⁰ *State Bank v. Moline Pressed Steel Co.*, 208 Ill. App. 412.

³¹ *Hitchcock v. American Pipe & Construction Co.*, 90 N. J. Eq. 576, 107 Atl. 267, rev'g 89 N. J. Eq. 440, 105 Atl. 655.

³² *Charles H. Welling Co. v. Platt*, — N. Y. Misc. —, 173 N. Y. Supp. 460.

³³ Opening defaults, see § 3119, *supra*.

³⁴ *Duquesne Bond Corporation v. American Surety Co. of New York*, 264 Pa. 203, 107 Atl. 759.

Judgment against predecessor as binding on company, see *Hudson v. Ukiah Water Improvement Co.*, 177 Cal. 498, 171 Pac. 93.

³⁵ A corporation which, although

not a party to the record, takes part in and manages the litigation, is bound by the judgment the same as a party. *Searchlight Horn Co. v. American Graphophone Co.*, 240 Fed. 745.

A corporation which defends a suit against another corporation which has gone out of existence, without urging the misnomer, is bound by the judgment. *Auglaize Box Board Co. v. Hinton*, 100 Ohio St. 505, 126 N. E. 881.

³⁶ *Scandia State Bank of Fergus Falls, Minnesota v. Dinnie*, — N. D. —, 172 N. W. 62.

³⁷ *Cedar Rapids Cold Storage Co. v. Lesinger*, — Iowa —, 177 N. W. 548.

Stockholders are sometimes held bound by judgments against the corporation although not made parties to the action;³⁸ but the fact that a person is a large or majority stockholder in a corporation does not make him a party to an action by or against the corporation within the rule requiring, *inter alia*, identity of parties to make a judgment in one proceeding *res judicata* in another.³⁹ Judgment against a corporation in an action wherein corporate existence was alleged and not denied by the other party is conclusive in regard thereto in contempt proceedings against a corporate officer for violating the judgment.⁴⁰ A judgment in a stockholders' suit as representing the corporation is no bar to an action by the stockholder on a cause of action accruing to him as an individual.⁴¹ A judgment in favor of defendant corporation does not inure to the benefit of the person who organized the corporation to carry on his own business, so as to bar a second suit against him individually for the injuries.⁴²

A receiver is not bound by an adjudication to which he is not a party,⁴³ but he is bound by a judgment against the corporation in an action defended by him.⁴⁴

§ 3125. Appeal and review. Directors vested with legal title to the property involved have power to prosecute a writ of error.⁴⁵ Notice of appeal must be served on defendant stockholders as well as on defendant corporation.⁴⁶ Notice of appeal is ineffective where not served on the proper agent of a foreign corporation.⁴⁷

³⁸ *Marin v. Augedahl*, 247 U. S. 142, 62 L. Ed. 1038; *Keyes v. Baskerville*, — S. D. —, 175 N. W. 874. See *Cuneo Importing Co. v. American Importing & Transportation Co.*, 247 Fed. 413.

³⁹ *Macan v. Scandinavia Belt-ing Co.*, 264 Pa. 384, 5 A. L. R. 1502, 107 Atl. 750.

⁴⁰ *Drew v. Superior Court of California in and for Mendocino County*, — Cal. App. —, 190 Pac. 374.

⁴¹ *Higgins v. Applebaum*, 186 N. Y. App. Div. 682, 174 N. Y. Supp. 807.

⁴² *McAlevey v. Litch*, — Mass. —, 125 N. E. 606.

⁴³ *In re New York Municipal E. Co.*, 189 N. Y. App. Div. 814, 179 N. Y. Supp. 238.

⁴⁴ *MacDonald v. Aetna Indemnity Co.*, — Conn. —, 105 Atl. 470.

⁴⁵ *Leyhe v. Leyhe*, — Tex. Civ. App. —, 220 S. W. 377.

⁴⁶ *Thwing v. MacDonald*, 139 Minn. 157, 165 N. W. 1065.

⁴⁷ *Roe v. Jewell Tea Co.*, — Ind. App. —, 124 N. E. 505.

CHAPTER 48

ATTACHMENT, GARNISHMENT, EXECUTION, CREDITORS' BILLS AND SUPPLEMENTARY PROCEEDINGS

I. ATTACHMENT, GARNISHMENT AND EXECUTION

A. By and Against Corporations Generally

§ 3128. Against domestic corporations.

§ 3129. Against foreign corporations—Attachment in general.

C. Stock and Stockholders and Corporate Bonds

§ 3145. Enforcement of statutory or subscription liability of stockholder.

D. Particular Classes of Corporations

§ 3171. Public service corporations generally.

E. Insolvency, Dissolution and Receivership

§ 3183. Effect of receivership—Property of foreign corporation.

F. Practice and Procedure

§ 3189. Affidavits—Attachment by corporation—Who may make.

§ 3192. — Attachment against corporation—Foreign corporation.

§ 3194. Service or levy—In general.

§ 3195. — On domestic corporation.

§ 3198. Return of service.

II. CREDITORS' BILLS AND BILLS IN AID OF EXECUTION

§ 3205. Right of creditor to maintain bill.

§ 3206. Conditions precedent.

§ 3207. Parties.

III. SUPPLEMENTARY PROCEEDINGS

§ 3208. Statutory provisions.

§ 3212. Procedure.

I. ATTACHMENT, GARNISHMENT AND EXECUTION

A. By and Against Corporations Generally

§ 3128. Against domestic corporations.¹

¹ Action against new corporation as based on contract, so as to as successor of the lessee, for rent, authorize attachment, see Stan-

§ 3129. **Against foreign corporations—Attachment in general.** That defendant is a foreign corporation is a ground for attachment in some states.² A foreign corporation is subject to attachment, under the New York statutes, merely because it is a foreign corporation, and it is immaterial that it has been duly authorized to transact business in the state.³ Acceptance of service of summons, and an appearance, by a foreign corporation, does not affect the validity of an attachment of the property of the corporation, so far as irregularities are concerned.⁴ For the purpose of jurisdiction in attachment suits against foreign corporations, the situs of the debt is the domicile of the garnishee.⁵

*C. Stock and Stockholders and Corporate Bonds*⁶

§ 3145. **Enforcement of statutory or subscription liability of stockholder.** Limitations do not begin to run against garnishment proceedings by a creditor to enforce unpaid subscriptions until execution issued on a judgment against the corporation is returned nulla bona.⁷

D. Particular Classes of Corporations

§ 3171. **Public service corporations generally.** Property of quasi public corporations which cannot be sold without interfering with the rights of the public is not subject to execution.⁸

ford Hotel Co. v. H. Schwind Co., — Cal. —, 181 Pac. 780.

² See Colcord v. Banco De Tam-aulipas, 191 N. Y. App. Div. 94, 180 N. Y. Supp. 852; Sorensen v. S. A. Companhia General Commercial de Santos, Santos, Brazil, — N. Y. App. Div. —, 180 N. Y. Supp. 201, as to sufficiency of complaint and affidavit to show defendant a foreign corporation; Lehigh Coal & Navigation Co. v. Skeele Coal Co., 265 Pa. 534, 109 Atl. 160.

³ Prentiss v. Greene, 193 N. Y. App. Div. 672, 184 N. Y. Supp. 558.

⁴ Lester v. Fox Film Co., — S. C. —, 103 S. E. 775.

⁵ Illinois Trust & Savings Bank v. Northern Bank & Trust Co., 214 Ill. App. 440.

⁶ See §§ 3436-3444, *infra*.

⁷ Lake Jackson Hotel Co. v. Rodwell, 202 Ala. 216, 80 So. 38.

⁸ Eldredge v. Mill Ditch Co., 90 Ore. 590, 177 Pac. 939.

Property of a mutual water company, which is in effect a holding company for irrigating rights, is not subject to execution. Eldredge v. Mill Ditch Co., 90 Ore. 590, 177 Pac. 939.

E. Insolvency, Dissolution and Receivership

§ 3183. Effect of receivership—Property of foreign corporation. Funds of a foreign bank held in Illinois may be garnished by a resident of Illinois although the bank is insolvent and in the hands of a receiver.⁹

F. Practice and Procedure

§ 3189. Affidavits—Attachment by corporation—Who may make. An affidavit for attachment signed by a corporate name “per W. L. Gooding, Agent” is sufficient where the body of the affidavit shows that it was made by such agent.¹⁰

§ 3192. — Attachment against corporation—Foreign corporation. Whether or not a bare allegation that defendant is a foreign corporation is sufficient to support an attachment, under the New York statutes, it is sufficient where the company itself stated in the contract sued on that it was of Brazil.¹¹

§ 3194. Service or levy—In general. In Georgia, the rule as to service on corporations in cases of garnishment is not the same as in ordinary suits maintained against them.¹² In Michigan, under the new Judicature Act, service of process in garnishment should be made on the same persons as is provided for in the service of process generally on corporations.¹³

§ 3195. — On domestic corporation.¹⁴ In Georgia a garnishment summons may be served, in case of domestic corporations, “upon the agent in charge of the office or business of the corporation.” The president is such an agent but a cashier of a bank is not necessarily such an agent.¹⁵

⁹ Illinois Trust & Savings Bank v. Northern Bank & Trust Co., 292 Ill. 11, 126 N. E. 533.

¹⁰ East Side Packing Co. v. Meritz, — Mo. App. —, 213 S. W. 436.

¹¹ Sorensen v. S. A. Companhia General Commercial de Santos, Santos, Brazil, — N. Y. Misc. —, 180 N. Y. Supp. 201.

¹² North Georgia Banking Co. v. Fancher, 23 Ga. App. 683, 99 S. E. 228.

¹³ Drueke-Lynch Co. v. Corson, 204 Mich. 180, 170 N. W. 43.

¹⁴ Sufficiency of service on corporation of execution against wages of an employee, as depending on person or officer served, see Starke v. S. G. Beckwith Special Agency, 227 N. Y. 42, 124 N. E. 96, rev'g 176 N. Y. App. Div. 910, 162 N. Y. Supp. 1145.

¹⁵ North Georgia Banking Co. v. Fancher, 23 Ga. App. 683, 99 S. E. 228.

§ 3198. Return of service. The garnishment return must show that the person served was the agent in charge of the office or business unless the official served, such as the president, is *prima facie* and as a matter of law the alter ego of such corporation by virtue of such office.¹⁶

II. CREDITORS' BILLS AND BILLS IN AID OF EXECUTION

§ 3205. Right of creditor to maintain bill. In some states the statutes expressly provide for so-called "sequestration" proceedings where an execution against a corporation is returned unsatisfied.¹⁷ A creditor's bill seeking to follow corporate assets in the hands of all who are not bona fide purchasers is not multifarious.¹⁸ A judgment creditor's action against a new company as successor of the old, the judgment debtor, on the theory that the new corporation was organized to defraud judgment creditors, is one based on fraud within the five-year statute of limitations.¹⁹

§ 3206. Conditions precedent. Where a creditor has a trust in his favor, as where the debtor corporation has in its hands funds devoted to the payment of creditors and transferred to it in violation of a trust devolved on a committee appointed to manage the corporation, equity has jurisdiction for diversion of the trust fund without first obtaining a judgment at law.²⁰

§ 3207. Parties. In a judgment creditor's suit against a corporation, it is proper to join officers of the corporation claimed to have unlawfully obtained property of the corporation.²¹

¹⁶ North Georgia Banking Co. v. Fancher, 23 Ga. App. 683, 99 S. E. 228.

¹⁷ John Miller Co. v. Harvey Mercantile Co., 38 N. D. 531, 165 N. W. 558, holding that all officers and stockholders and other persons who have incurred a liability to the corporation may be joined as defendants.

¹⁸ Hoggan v. Price River Irriga-

tion Co., — Utah —, 184 Pac. 536.

¹⁹ Walker v. Ozark Cooperage & Lumber Co., — Mo. App. —, 218 S. W. 694.

²⁰ Kentucky Wagon Mfg. Co. v. Jones & Hopkins Mfg. Co., 248 Fed. 272.

²¹ Taylor v. Ellsworth Building Corporation, — N. Y. Misc. —, 183 N. Y. Supp. 394.

III. SUPPLEMENTARY PROCEEDINGS

§ 3208. **Statutory provisions.** Property in the hands of a corporation may be reached by supplementary proceedings against an individual.²²

§ 3212. **Procedure.** Failure of the president to appear in supplementary proceedings, as required by the order, is a contempt.²³ In New York, the president of a dissolved corporation may be required to appear in supplementary proceedings against the corporation.²⁴ A resignation as director is not effective so as to prevent service in supplementary proceedings where such resignation was part of a fraudulent scheme to prevent the collection of the judgment.²⁵

²² *Deer Island Lumber Co. v. Virginia-Carolina Chemical Co.*, 111 S. C. 299, 97 S. E. 833.

²³ *Drew v. Superior Court*, — Cal. —, 182 Pac. 417.

²⁴ *Sanitary Brass Works v. Rubin & Marcus*, 110 N. Y. Misc. 565, 180 N. Y. Supp. 619.

²⁵ *Inventions Corporation v. Hobbs*, 244 Fed. 430.

CHAPTER 49

QUO WARRANTO

II. WHEN REMEDY AVAILABLE

- § 3226. Purpose and propriety of remedy generally—Corporations as “persons” within quo warranto statutes.
- § 3227. Determination of corporate existence and powers.
- § 3232. Ouster of foreign corporations.
- § 3235. Effect of existence of other remedies—Remedy under criminal laws.

III. PROCEDURE

- § 3236. Jurisdiction and venue.
- § 3240a [New]. Parties plaintiff—Corporation as proper relator.
- § 3241. —Right and duty of public officers to institute proceedings.
- § 3242. Parties defendant.
- § 3255. Information or complaint—Alleging usurpation.
- § 3265. Evidence.

II. WHEN REMEDY AVAILABLE

§ 3226. Purpose and propriety of remedy generally—Corporations as “persons” within quo warranto statutes.¹

§ 3227. Determination of corporate existence and powers. Quo warranto is the proper remedy where a corporation practiced fraud in obtaining its charter.² Legality of corporate existence can be challenged only by quo warranto and not by an injunction suit.³ The state may attack the constitutionality of the statute under which a company claims to be incorporated.⁴

§ 3232. Ouster of foreign corporations. Quo warranto is not the remedy to exclude an industrial insurance company of a sister state from doing business in Alabama.⁵

¹ See § 54, *supra*.

² *State v. Senatobia Blank Book & Stationery Co.*, 115 Miss. 254, 76 So. 258.

³ *Nelson v. Consolidated Inde-*

pendent School Dist., 181 Iowa 424, 164 N. W. 874.

⁴ *Bush v. State ex rel. Werneke*, 187 Ind. 339, 119 N. E. 417.

⁵ *State ex rel. Dallas v. Atlanta*

§ 3235. Effect of existence of other remedies—Remedy under criminal laws. Quo warranto proceedings are civil rather than criminal.⁶

III. PROCEDURE

§ 3236. Jurisdiction and venue. Quo warranto to forfeit the franchise may be brought in any county.⁷ Quo warranto against a national bank may be brought in a state court by the state attorney general, where involving a federal statute which impliedly authorizes such procedure.⁸

§ 3240a [New]. Parties plaintiff—Corporation as proper relator. The corporation is a proper relator in quo warranto to oust individual respondents from franchises alleged to be usurped in the corporation.⁹

§ 3241. — Right and duty of public officers to institute proceedings. The right of the attorney general to act for the state in such inquiry comes from the common law.¹⁰

§ 3242. Parties defendant.¹¹ Officers of the corporation need not be made parties to an action for forfeiture of the franchise for failure to comply with statutes.¹²

Mut. Ins. Co., 200 Ala. 443, 76 So. 375.

⁶ State ex rel. Langer v. Gamble-Robinson Fruit Co., — N. D. —, 176 N. W. 103, quoting Fletcher Cyc. Corp. § 3235.

⁷ State ex rel. Chamberlain v. Public Drug Co., 41 S. D. 287, 170 N. W. 161.

⁸ First Nat. Bank of Bay City v. Union Trust Co., 244 U. S. 416, 61 L. Ed. 1233, L. R. A. 1918 C 283, rev'g 192 Mich. 640, 159 N. W. 335.

⁹ State ex rel. Northwestern Colonization & Improvement Co. v. Huller, 23 N. M. 306, 1 A. L. R. 170 with note, 168 Pac. 528.

¹⁰ State ex rel. Langer v. Gamble-Robinson Fruit Co., — N. D. —, 176 N. W. 103, citing Fletcher Cyc. Corp. § 3241.

¹¹ Lowery v. Mutual Loan Society, 202 Ala. 51, 79 So. 389.

Notes on "Joinder of parties in quo warranto proceedings," see Ann. Cas. 1918 D 214; on "Proper parties defendant in quo warranto proceedings against corporations," see Ann. Cas. 1918 D 228.

¹² State ex rel. Chamberlain v. Public Drug Co., 41 S. D. 287, 170 N. W. 161.

§ 3255. Information or complaint—Alleging usurpation. The information in quo warranto proceedings to oust a corporation must state facts to show that there was no legal incorporation as claimed.¹³

§ 3265. Evidence. In quo warranto brought on the relation of both the state's attorney and of a private person, to forfeit a charter, the interest of the private person need not be shown.¹⁴

¹³ Bush v. State ex rel. Werneke, Public Drug Co., 41 S. D. 287, 170 187 Ind. 339, 119 N. E. 417. N. W. 161.

¹⁴ State ex rel. Chamberlain v.

CHAPTER 50

MANDAMUS

I. GENERAL CONSIDERATIONS

§ 3277. The remedy in general.

II. ACTS AS TO WHICH REMEDY MAY BE INVOKED

§ 3279. Duties arising out of contracts.

§ 3289. Restoration of membership in association or society.

§ 3291. Issuance of certificates of stock.

III. APPLICATION OF REMEDY TO PARTICULAR CLASSES OF CORPORATIONS

§ 3295. Public service corporations—In general.

§ 3301. — Gas and heating companies.

§ 3303. — Railroads.

§ 3304. — Street railroads.

§ 3305. — Telephone companies.

IV. PROCEDURE

§ 3311. Pleading.

I. GENERAL CONSIDERATIONS

§ 3277. **The remedy in general.** Mandamus lies, in a proper case, to compel a superintendent of banks to issue a charter to a bank.¹

II. ACTS AS TO WHICH REMEDY MAY BE INVOKED

§ 3279. **Duties arising out of contracts.** A stockholder cannot, by mandamus, compel his corporation to enter into a contract.²

¹ Mulkey v. Bennett, 95 Ore. 70, 186 Pac. 1115.

² Burgess Stock Farm v. Percheron Society, 212 Ill. App. 132.

§ 3289. Restoration of membership in association or society. Mandamus lies to compel reinstatement of a member of a beneficial association, where expelled without valid trial.³

§ 3291. Issuance of certificates of stock. Mandamus lies to compel the issuance of certificates of stock to persons entitled thereto, and recordation of ownership on corporate books.⁴

III. APPLICATION OF REMEDY TO PARTICULAR CLASSES OF CORPORATIONS

§ 3295. Public service corporations—In general. Mandamus lies in favor of a city to compel a public service company to make reports to be used in fixing rates.⁵ A stranger cannot, by mandamus, raise the question whether a franchise exists entitling a company to use streets.⁶

§ 3301. — Gas and heating companies. Mandamus lies to compel a gas company to make connections.⁷

§ 3303. — Railroads. Mandamus lies to compel a railroad company to perform a public duty.⁸

§ 3304. — Street railroads. Mandamus is the proper remedy to compel a street railroad company to operate its cars,⁹ but mandamus does not lie against a street car company to compel it to continue service where the service has not yet been discontinued.¹⁰ Mandamus does not lie to compel construction of a

³ *Lazic v. National Croation Soc. of United States of America*, 260 Pa. 205, 103 Atl. 588.

⁴ *Capitol Petroleum Co. v. Hal-deman*, — Colo. —, 180 Pac. 758, citing *Fletcher v. Cyc. Corp.* § 3291, and see § 3818, *infra*.

⁵ *Tampa Waterworks Co. v. State*, — Fla. —, 82 So. 230.

⁶ *Clements v. Williams*, 191 N. Y. App. Div. 279, 181 N. Y. Supp. 230.

⁷ *Public Service Commission v.*

Iroquois Nat. Gas Co., 108 N. Y. Misc. 696, 178 N. Y. Supp. 24.

⁸ *State ex rel. Public Service Commission v. Missouri Southern R. Co.*, 279 Mo. 455, 214 S. W. 381.

⁹ *State of Washington ex rel. City of Seattle v. Puget Sound Traction, Light & Power Co.*, 243 Fed. 748.

¹⁰ *State ex rel. Lawton v. Public Service Commission*, — Nev. —, 190 Pac. 284.

street railway from terminus to terminus where it cannot obtain the right to cross a steam railway on its route.¹¹

§ 3305. — **Telephone companies.** Mandamus does not lie to compel physical connection of telephone lines where there is a plain and adequate remedy by application to the Kansas court of industrial relations.¹²

IV. PROCEDURE

§ 3311. Pleading.¹³

¹¹ Hamilton Tp. v. Mercer Ass'n v. Southwestern Bell Tel. County Traction Co., 90 N. J. L. Co., — Kan. —, 190 Pac. 747.
331, 102 Atl. 3.

¹³ See § 2846, supra.

¹² Clay County Co-Op. Tel.

CHAPTER 51

INJUNCTIONS

- § 3316. Character of damage, irreparable injury, etc.
- § 3317. Preliminary and interlocutory injunctions.
- § 3320. Ultra vires acts—Right of state to enjoin.
- § 3321. — Right of third person to enjoin.
- § 3322. — Internal affairs of corporation.
- § 3325. Title to corporate office.
- § 3329. Violation of corporate franchise.
- § 3330. Failure of corporation to discharge franchise obligations.
- § 3334. Parties defendant.

§ 3316. Character of damage, irreparable injury, etc. A corporate election by a rival faction will not be enjoined where no irreparable injury is threatened.¹ Where the question of control of the corporation is involved, the remedy at law for damages for an improper sale of stock to a director may be entirely inadequate, and where fraud on the part of the managing officers is alleged, equity has jurisdiction to inquire into the transaction and make such a decree as the circumstances may warrant.²

§ 3317. Preliminary and interlocutory injunctions. The wealth of plaintiff corporation is of little importance in determining the amount of an injunction bond required.³

§ 3320. Ultra vires acts—Right of state to enjoin. The public service commission may enjoin a manufacturing company from distributing electricity without the approval of such commission, where the statute under which it was incorporated confers no such authority.⁴

¹ *Planters' Hotel v. Stewart*, 145 La. 370, 82 So. 374.

Kildare Club, 186 N. Y. App. Div. 852, 174 N. Y. Supp. 769.

² *Glenn v. Kittanning Brewing Co.*, 259 Pa. 510, L. R. A. 1918 D 738, 103 Atl. 341.

⁴ *Public Service Commission v. J. & J. Rogers Co.*, 103 N. Y. Misc. 711, 170 N. Y. Supp. 964.

³ *A. Sherman Lumber Co. v.*

§ 3321. — **Right of third person to enjoin.** Injunction lies to prevent a competitor public utility using the streets without a legal franchise.⁵

§ 3322. **Internal affairs of corporation.** Internal affairs of a corporation will not ordinarily be interfered with by injunction.⁶ Motives of the directors will not be considered in the injunction suit.⁷

§ 3325. **Title to corporate office.** A discharged officer may be restrained by injunction from acting as such officer.⁸

§ 3329. **Violation of corporate franchise.**⁹ A public service corporation may enjoin acts of a city violating its contract with the city by making a contract with a rival company.¹⁰ Injunction lies to prevent a municipality obstructing a street car line,¹¹ or unlawfully operating 'bus and stage lines on its streets.¹² A street railway company with a franchise to use city streets may enjoin the use of such streets by jitneys and the threatened enforcement of an ordinance for licensing jitneys.¹³ A street railway company may enjoin the tearing up of its tracks while a sewer is being laid, where the recovery of damages would be inadequate.¹⁴

A city may be enjoined from erecting a competing light plant in violation of its contract with the corporation.¹⁵ An injunction

⁵ Springfield Gas & Electric Co. v. Springfield, 292 Ill. 236, 126 N. E. 739; Farmers' & Merchants' Co-Op. Tel. Co. v. Boswell Tel. Co., 187 Ind. 371, 119 N. E. 513.

⁶ Thurmond v. Paragon Colliery Co., 82 W. Va. 49, 95 S. E. 816, and see § 4065, *infra*.

⁷ Haldeman v. Haldeman, 176 Ky. 635, 197 S. W. 376.

⁸ Henri Gutmann Silks Corporation v. Reilly, 189 N. Y. App. Div. 258, 178 N. Y. Supp. 457.

⁹ See also § 3321, *supra*.

¹⁰ Oconto Elec. Co. v. Oconto Service Co., 168 Wis. 165, 169 N. W. 293.

¹¹ Pottsville Union Traction Co. v. St. Clair Borough, 261 Pa. 293, 104 Atl. 602.

¹² Brooklyn City R. Co. v. Whalen, 191 N. Y. App. Div. 737, 182 N. Y. Supp. 283.

¹³ Lindsley v. Dallas Consol. St. Ry. Co., — Tex. Civ. App. —, 200 S. W. 207, quoting 4 McQuillin Mun. Corp. § 1771.

¹⁴ Public Service R. Co. v. Frazer, 87 N. J. Eq. 679, 102 Atl. 890.

¹⁵ Memphis Elec. Light, Heat & Power Co. v. City of Memphis, 271 Mo. 488, 196 S. W. 1113.

is proper to prevent interference with franchise rights by a competitor in violation of a statute prohibiting duplication of public service unless public necessity is shown.¹⁶

§ 3330. Failure of corporation to discharge franchise obligations. Injunction lies to prevent a public service company from cutting off light to a patron in violation of a contract.¹⁷

§ 3334. Parties defendant. Managing officers, as well as the corporation, may be enjoined from using the corporation for unfair competition.¹⁸

¹⁶ Farmers' & Merchants' Co. 4 McQuillin Mun. Corp. §§ 1773, Op. Tel. Co. v. Boswell Tel. Co., 1774.

¹⁷ Ind. 371, 119 N. E. 513.

¹⁸ Prest-O-Lite Co. v. Acetylene Welding Co., 259 Fed. 940.

¹⁷ Warmack v. Major Stave Co., 132 Ark. 173, 200 S. W. 799, citing

CHAPTER 52

LIABILITY OF CORPORATION FOR TORTS

I. NATURE AND EXTENT OF LIABILITY GENERALLY

- § 3336. Introductory.
- § 3337. Effect of legislative authority.
- § 3338. Torts involving intent and malice.
- § 3339. Defense of ultra vires.
- § 3340. Principles determining liability—In general.
- § 3341. — Liability by reason of ratification or adoption.
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- § 3343. — Conspiracy.
- § 3344. — Conversion.
- § 3345. — False arrest and imprisonment and malicious prosecution.
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- § 3352. — Torts of special police officers.
- § 3353. Joint and several liability of corporation and agent or servant.
- § 3354. Exemplary damages—In general.
- § 3355. — For what torts awarded.

III. CHARITABLE CORPORATIONS

- § 3363. Application of theories.

I. NATURE AND EXTENT OF LIABILITY GENERALLY

§ 3336. **Introductory.**¹ A corporation is liable for torts in a proper case.²

§ 3337. **Effect of legislative authority.**³ A public service corporation acting in its public, as distinguished from private,

¹ Federal control as affecting liability, see *Spring v. American Telegraph & Telephone Co.*, — W. Va. —, 103 S. E. 206. eleemosynary corporations, see 5 Cornell L. Q. 409-423; 6 Cornell L. Q. 56-84.

Respondent superior as applied in New York to quasi public and ² *United Mine Workers v. Coronado Coal Co.*, 258 Fed. 829.

³ See also § 3349, *infra*.

capacity, is not liable for damages, unless imposed by statute, in locating, constructing or changing the construction, or in the operation, of its works.⁴ A public service corporation is not liable in trespass for placing poles on private property where done under the direction of the highway engineer who purported to locate them in the public highway.⁵

§ 3338. Torts involving intent and malice. A corporation may be guilty of malice, through its servants, in molesting a person in the exercise of his calling.⁶

§ 3339. Defense of ultra vires. Ultra vires is no defense in a tort action.⁷ Thus, a corporation may be held liable for conspiracy to defraud even though the transaction by means of which the fraud was accomplished was outside the scope of its corporate powers.⁸ In any event negligence of a furniture company in hanging a swing sold a customer cannot be defended on the ground that its act was ultra vires, since such act was clearly not ultra vires.⁹

§ 3340. Principles determining liability—In general.¹⁰ In California the rule is stated that a corporation is liable "for the torts of its servant, if such servant has authority from it to do

⁴ Killam v. Norfolk & W. R. Co., 122 Va. 541, 6 A. L. R. 701, 96 S. E. 506.

⁵ Brammer v. Iowa Tel. Co., 182 Iowa 865, 1 A. L. R. 400 (with note on "Authority from public official as affecting responsibility of public service corporation for infringing property rights"), 165 N. W. 117.

⁶ Pratt v. British Medical Ass'n, [1919] 1 K. B. 244, 279.

⁷ Panama R. Co. v. Curran, 256 Fed. 768; Arthur Wagner Co. v. Gallaher, 204 Ill. App. 206; Start v. National Newspaper Ass'n, — Mo. App. —, 222 S. W. 870; Basil v. Spratt, 45 Dom. L. Rep. (Can.) 554.

⁸ Brumley v. Chattanooga Speed-

way & Motordrome Co., — Tenn. —, 198 S. W. 775.

⁹ Rick Furniture Co. v. Smith, — Tex. Civ. App. —, 202 S. W. 99.

¹⁰ A corporation is not liable for the tort of an employee in starting a fire where not within the scope of his employment. Archuleta v. Floersheim Mercantile Co., 25 N. M. 632, 187 Pac. 272.

A corporation is not liable for the wrongful discharge of an employee by its general manager, where without authority, unless it has ratified the discharge. Birmingham Realty Co. v. Hale, 16 Ala. App. 460, 78 So. 723.

the tortious act, but not otherwise.”¹¹ The “law of the federal courts is clear that, in order to hold a corporation liable for the negligence of its agents, the act in question must be performed in the course of the agent’s employment in the business of the principal.”¹² Corporations are liable for torts “of their members or employees, when encouraged in the commission of them, or if ratified thereafter.”¹³ A corporation is liable for a tort although no person was authorized to so conduct the corporate business as to impose on it liability for negligence or other tort.¹⁴

A board of trade or exchange is not liable for acts of its directors in fining and suspending a member, where the directors themselves were not liable.¹⁵ A water company is liable for the wrongful act of its general manager in cutting off the water supply to a customer to force the payment of a debt.¹⁶

That a corporation is a stockholder in another corporation does not make it liable for torts of the latter.¹⁷ But a corporation is liable for a tort where it controlled and conducted a business through another company in the operation of which the injury occurred.¹⁸

§ 3341. — Liability by reason of ratification or adoption.¹⁹ A tort of a servant is ratified by accepting the benefits thereof.²⁰

§ 3342. — Assault and battery. A corporation may be held liable in damages for an assault and battery.²¹ A transfer com-

¹¹ *Conceoff v. Hippodrome Theater Co.*, — Cal. —, 182 Pac. 273.

¹² *Gorham v. Cunard S. S. Co.*, 254 Fed. 716, 719.

¹³ *United Mine Workers v. Coronado Coal Co.*, 258 Fed. 829, 837.

¹⁴ *Clinchfield Fuel Co. v. Henderson Iron Works Co.*, 254 Fed. 411.

¹⁵ *Melady v. South St. Paul Live Stock Exchange*, 142 Minn. 194, 171 N. W. 806.

¹⁶ *Eutaw Ice Water & Power Co. v. McGee*, 16 Ala. App. 652, 81 So. 144.

¹⁷ *Friedman v. Vandalia R. Co.*, 254 Fed. 292.

¹⁸ *United Laundries Co. v. Bradford*, — Conn. —, 105 Atl. 303; *Auglaize Box Board Co. v. Hinton*, 100 Ohio St. 505, 126 N. E. 881.

¹⁹ Sufficiency of evidence of ratification of slander, see *Buckeye Cotton Oil Co. v. Sloan*, 250 Fed. 712, 725; *Vowles v. Yakish*, — Iowa —, 179 N. W. 117.

²⁰ *Kirk v. Montana Transfer Co.*, 56 Mont. 292, 184 Pac. 987.

²¹ *Louisville & N. R. Co. v. Lacey*, — Ala. App. —, 82 So. 636; *Empire Clothing Co. v. Hammons*, — Ala. App. —, 81 So. 838, sufficiency of complaint.

pany is liable for an assault committed by its teamster while moving household goods, where acting within the scope of his authority.²²

§ 3343. — Conspiracy. A corporation is liable in damages for civil conspiracy in which it participated.²³ To bind a corporation "for damages caused by such conspiracy, it is not necessary for the officers or agents through whom the corporation acts and did act to have had authority to perform all the acts done in the execution of the conspiracy, or agreed to be performed by other confederates in the execution of the conspiracy," but "as to any essential fact which the conspiracy contemplated and which it was agreed that the agent of the corporation should do, it is necessary that such act agreed upon by the corporation be in fact done by its agent for such corporation, and that, while so doing, the agent was acting within the line and scope of his employment by such corporation and in the prosecution of its business."²⁴

§ 3344. — Conversion. A bank is not liable for misappropriation of funds by its cashier where the money was turned over to the cashier by a depositor to be loaned by the cashier as an individual and agent of the depositor.²⁵

§ 3345. — False arrest and imprisonment and malicious prosecution. Authorized act of a corporate agent in arresting one of the corporate employees is the act of the corporation so as to make it liable for malicious prosecution.²⁶ A railroad company is liable for malicious prosecution for the act of a station agent and yardmaster in instituting a criminal prosecution

²² *Kirk v. Montana Transfer Co.*, 56 Mont. 292, 184 Pac. 987.

²³ *National Park Bank of New York v. Louisville & N. R. Co.*, 199 Ala. 192, 74 So. 69; *Brumley v. Chattanooga Speedway & Motor-drome Co.*, — Tenn. —, 198 S. W. 775.

Liability for conspiracy between arms company and labor union, see *United Mine Workers*

v. Coronado Coal Co., 258 Fed. 829.

²⁴ *National Park Bank of New York v. Louisville & N. R. Co.*, 199 Ala. 192, 74 So. 69.

²⁵ *Holmes v. Uvalde Nat. Bank*, — Tex. Civ. App. —, 222 S. W. 640.

²⁶ *Western U. Tel. Co. v. Thom-
asson*, 251 Fed. 833.

against a consignee of goods to regain the shipment, where the agent was authorized to hold the shipment until charges were paid, notwithstanding the method of regaining the goods was unauthorized.²⁷

On the other hand, a store corporation is not liable for false imprisonment where its general manager and detective merely charged plaintiff with theft, where they took no part in his detention by a police detective who proceeded on his own initiative and judgment.²⁸ So there is no implied authority of an usher in a theater to arrest or imprison persons who might commit criminal offenses while in the theater, and hence the theater company is not liable for false imprisonment because of such act.²⁹

§ 3346. — Fraud and deceit. Misrepresentations of corporate officers are imputable to the corporation.³⁰

§ 3347. — Libel and slander. A corporation may be sued for libel³¹ provided the libel was within the scope of the employment of the offending officer or employee.³² Corporations "are liable for libel and slander, uttered by their officers and agents in the scope of their employment, the same as other torts."³³ A

²⁷ Chicago, R. I. & P. R. Co. v. Gage, 136 Ark. 122, 206 S. W. 141.

²⁸ Zinkfein v. W. T. Grant Co., — Mass. —, 128 N. E. 24.

²⁹ Concoff v. Hippodrome Theater Co., — Cal. —, 182 Pac. 273.

³⁰ Brady v. Cobbs, — Tex. Civ. App. —, 211 S. W. 802.

³¹ Stanley v. Sangerville, — Me. —, 109 Atl. 189; Barger v. Hood, — W. Va. —, 104 S. E. 280, holding that the authority of the officer or agent need not be pleaded; Morse v. Modern Woodmen of America, 166 Wis. 194, Ann. Cas. 1918 D 480, 164 N. W. 829.

In a libel suit against a corporation, letters purporting to have been sent by it are not admissible to show the libel where the

authority of the signer to act for the corporation is not proved. Garrett v. Locke Regulator Co., — N. Y. Misc. —, 167 N. Y. Supp. 64.

Stockholders are not guilty of libel where they circulate only among other stockholders a letter attacking the acts of a director as such, since a privileged communication. La Plant v. Hyman, — Colo. —, 180 Pac. 83.

³² Sullivan v. Metropolitan Casualty Ins. Co., 256 Fed. 726.

An insurance adjuster is not acting within the scope of his authority in charging the insured with arson where the company was not seeking release on that ground. Vowles v. Yakish, — Iowa —, 179 N. W. 117.

³³ Ecuyer v. New York Life

publishing corporation is liable for libel where its editor accepts and prints a malicious libel in the course of his employment, intentionally or without proper inquiry.³⁴ A station agent is not acting within the scope of his employment, so as to make the railroad company liable for libel, in circulating a rumor that plaintiff had stolen an overcoat of a newsboy on a train.³⁵ There is no publication of a libel by a corporation where it merely mails a letter from one of its branch offices to another.³⁶ The fact that plaintiff is a corporation does not affect the rule raising a presumption of damages from the use of prejudicial words libelous per se.³⁷

A corporation is liable for slander where the words are uttered by express authority of the company or within the course and scope of the agent's employment.³⁸ But in Georgia a corporation is not liable for slander unless the agent was expressly directed or authorized by the corporation to speak the words in question.³⁹ It is now definitely held in Massachusetts that a corporation is liable for slanderous words uttered by an officer, agent or servant in the course of his employment, and that they need not be uttered by the direct authority of the stockholders or directors.⁴⁰

Ins. Co., 107 Wash. 411, 181 Pac. 871.

³⁴ *Corrigan v. Bobbs-Merrill Co.*, 228 N. Y. 58, 10 A. L. R. 662, 126 N. E. 260.

³⁵ *Beaumont, S. L. & W. Ry. Co. v. Daniels*, — Tex. Civ. App. —, 204 S. W. 481.

³⁶ *Prins v. Holland-North America Mortg. Co.*, 107 Wash. 206, 5 A. L. R. 451, 181 Pac. 680.

Communication from home office to branch as libel, see note in 5 A. L. R. 455, annotating *Prins v. Holland-North America Mortg. Co.*, 107 Wash. 206, 5 A. L. R. 451, 181 Pac. 680.

³⁷ *Cotton Lumber Co. v. La Crosse Lumber Co.*, 200 Mo. App. 7, 204 S. W. 957.

³⁸ *Margolis v. United Dairy Co.*, 214 Ill. App. 613; *Vowles v. Yakish*, — Iowa —, 179 N. W. 117; *Cotton v. Fisheries Product*

Co., 177 N. C. 56, 97 S. E. 712.

A corporation "is liable for a slander by its agent when uttered within the scope of his employment and in the performance of his duties in the course of transacting the business of the corporation." Liability is not limited to express authorization of the slanderous words or words necessarily spoken in the course of the agent's duty. *Buckeye Cotton Oil Co. v. Sloan*, 250 Fed. 712, 719, disapproving *Southern Ice Co. v. Black*, 136 Tenn. 391, 397, Ann. Cas. 1917 E 695, 189 S. W. 861.

³⁹ *Headley v. Maxwell Motor Sales Co.*, — Ga. App. —, 102 S. E. 374.

⁴⁰ *Mills v. W. T. Grant Co.*, 233 Mass. 140, 123 N. E. 618, holding also that the same rule applies to libels.

In slander, the agent's authority need not be in writing under seal nor evidenced by a vote of the corporation, but it may be shown by extrinsic facts.⁴¹ Statements made to a personal friend on a social visit are not made within the scope of an agent's duty so as to make the corporation liable for slander.⁴² A corporation is not liable for slander by its agent merely because the defamatory words were used by him during negotiations entered into in the course of his duty.⁴³ An averment that slanderous words were spoken by a corporation necessarily implies that they were spoken by an agent or servant of the corporation.⁴⁴

§ 3348. — **Negligence.** Of course negligence of a corporation can be based only on negligence of some particular officer, agent or servant.⁴⁵ Corporations are liable for negligence under the law in force in the Canal Zone.⁴⁶ Rules of corporations cannot justify negligence.⁴⁷ It will be presumed, where an injury results from an automobile owned by a corporation and driven by its manager, that the latter was acting within the scope of his authority.⁴⁸

§ 3349. — **Nuisance.** Where a public service corporation acts in its private capacity, mere general legislative authority to establish, locate and operate its works will not confer on it immunity from liability for damages resulting from a construction and operation of such works, which would have been deemed a private nuisance at common law.⁴⁹ A railroad company using terminal yards to switch cars is not acting in its public capacity and is liable for a nuisance for damages to nearby property.⁵⁰

⁴¹ *Buckeye Cotton Oil Co. v. Bosse*, 249 U. S. 41, 63 L. Ed. 466. Sloan, 250 Fed. 712, 719.

⁴² *Buckeye Cotton Oil Co. v. Tex. Civ. App.* —, 210 S. W. 842. Sloan, 250 Fed. 712, 722.

⁴³ *Vowles v. Yakish*, — Iowa App. —, 182 Pac. 73. —, 179 N. W. 117.

⁴⁴ *Margolis v. United Dairy Co.*, 214 Ill. App. 613. Co., 122 Va. 541, 6 A. L. R. 701, 96 S. E. 506.

⁴⁵ *Miller v. Ann Arbor R. Co.*, 196 Mich. 297, 162 N. W. 1025. Co., 122 Va. 541, 6 A. L. R. 701, 96 S. E. 506.

⁴⁶ *Panama R. Co. v. Curran*, 256 Fed. 768, citing *Panama R. Co. v.*

§ 3351. — Wrongful death. A private corporation, although it may not be liable for the death of a person caused by negligence of its agents or employees, is liable for injuries resulting in death from what may be deemed its own wrongful acts or omissions as distinguished from the acts or omissions of its servants or agents.⁵¹ A construction corporation is not civilly liable for the act of its general manager in shooting and killing an employee after termination of a quarrel as to performance of his contract by the employee, since the shooting was not in the scope of the manager's employment.⁵²

§ 3352. — Torts of special police officers. The fact that one is a public officer does not preclude him from also acting in the capacity of an agent of a private corporation so as to make the latter liable for malicious prosecution because of his acts.⁵³ A corporation cannot, by securing, through others, special agents, even though they be officers of the law, for the prosecution of offenders around the plant, obtain any immunity from liability for malicious prosecutions which such owner would not be equally entitled to if it itself directly selected and paid the agents and expressly retained the power of control and removal.⁵⁴ A street car company is liable for false imprisonment where a conductor, whom it caused to be appointed a railroad policeman, illegally arrested a passenger for refusal to pay car fare, in the course of his employment.⁵⁵ Ratification of the acts of a police officer in making an arrest makes the corporation liable where such officer is also its agent.⁵⁶

§ 3353. Joint and several liability of corporation and agent or servant. Both the guilty officer or agent and the corporation are liable for publication of a libel.⁵⁷ A corporation is not

⁵¹ *Southwestern Portland Cement Co. v. Bustillos*, — Tex. Civ. App. —, 216 S. W. 268.

⁵² *Wells v. Henderson Land & Lumber Co.*, 200 Ala. 262, L. R. A. 1918 A 115, 76 So. 28.

⁵³ A corporation is liable for malicious prosecution instituted by an employee although he was also an employee of a private detective agency and a public offi-

cer. *Clinchfield Coal Corporation v. Redd*, 123 Va. 420, 96 S. E. 836.

⁵⁴ *Clinchfield Coal Corporation v. Redd*, 123 Va. 420, 96 S. E. 836.

⁵⁵ *La Chance v. Berlin St. Ry.*, — N. H. —, 109 Atl. 720.

⁵⁶ *Clinchfield Coal Corporation v. Redd*, 123 Va. 420, 96 S. E. 836.

⁵⁷ *Barger v. Hood*, — W. Va. —, 104 S. E. 280.

liable for false imprisonment where its general manager, who caused the arrest and is made a co-defendant, is exonerated.⁵⁸

§ 3354. Exemplary damages—In general. A corporation may be liable for punitive damages,⁵⁹ but not unless it has ratified the tort of its agent or servant or the tort-feasor is an alter ego of the corporation.⁶⁰ As affecting exemplary damages, the president of a corporation has no inherent power to direct a corporate employee to violate the law by committing a tort against the person or property of another.⁶¹

§ 3355. — For what torts awarded. Malice of its officer or agent may be imputed to a corporation, so as to authorize the recovery of exemplary damages, although the act was unauthorized, where the corporation sought to uphold the truth of the alleged libel and did not discharge the officer or agent.⁶²

III. CHARITABLE CORPORATIONS

§ 3363. Application of theories.⁶³ It is generally held that a charitable hospital is not liable to a patient for negligence of its employees, including nurses,⁶⁴ although the patient paid the regular rates charged pay patients.⁶⁵ In Georgia, however, the

⁵⁸ Vest v. S. S. Kresge Co., — Mo. App. —, 213 S. W. 165, holding rule not applicable.

⁵⁹ Beauchamp v. Winnsboro Granite Co., — S. C. —, 101 S. E. 856.

⁶⁰ Wortham-Carter Pub. Co. v. Littlepage, — Tex. Civ. App. —, 223 S. W. 1043.

⁶¹ Ketchum v. Amsterdam Apartments Co., — N. J. L. —, 110 Atl. 590.

⁶² Cotton Lumber Co. v. La Crosse Lumber Co., 200 Mo. App. 7, 204 S. W. 957.

⁶³ See generally Stewart v. California Medical Missionary & Benevolent Ass'n, — Cal. —, 176 Pac. 46.

What are charitable corporations, see § 100, supra.

⁶⁴ Paterlini v. Memorial Hospital Ass'n, 247 Fed. 639, Pennsylvania rule; Paterlini v. Memorial Hospital Ass'n, 241 Fed. 429.

⁶⁵ Burdell v. St. Luke's Hospital, 37 Cal. App. 310, 173 Pac. 1008; Nicholas v. Evangelical Deaconess Home & Hospital, — Mo. —, 219 S. W. 643.

Receiving pay from some of its patients does not affect the character of a hospital as a charitable corporation. Roosen v. Peter Bent Brigham Hospital, — Mass. —, 126 N. E. 392.

The fact that a large part of the revenue of a hospital is derived from pay patients does not destroy its character as a charitable corporation. Nicholas v.

rule is that a hospital, although a charitable corporation, is liable to a pay patient for negligence of an employee, but only to the extent of funds derived from non-charitable pay patients.⁶⁶ In Minnesota, a charitable corporation, whose hospital is more than self-supporting from pay patients, is liable to a patient for negligence of its employees.⁶⁷

Negligence in choosing incompetent or careless servants is not included within the exemption of charitable corporations from liability for negligence, it is held in New York.⁶⁸ In Massachusetts, however, such a corporation is not liable for negligence of managing officers in selecting incompetent servants.⁶⁹

This rule of exemption does not apply, it has been held, to the Modern Woodmen of America,⁷⁰ nor to a Y. M. C. A.,⁷¹ nor to a railway emergency hospital.⁷² It has been held applicable to educational institutions,⁷³ and to an Odd Fellows Home.⁷⁴

Nonliability of a hospital as a charitable corporation for negligence precludes liability under the death by wrongful act statute

Evangelical Deaconess Home & Hospital, — Mo. —, 219 S. W. 643.

⁶⁶ Morton v. Savannah Hospital, 148 Ga. 438, 96 S. E. 887.

⁶⁷ Mulliner v. Evangelischer Diakonniessenverein, etc., of German Evangelical Synod, 144 Minn. 392, 175 N. W. 699.

⁶⁸ Goodman v. Brooklyn Hebrew Orphan Asylum, 178 N. Y. App. Div. 682, 165 N. Y. Supp. 949.

⁶⁹ Roosen v. Peter Bent Brigham Hospital, — Mass. —, 126 N. E. 392.

⁷⁰ The Modern Woodmen of America, while having benevolent and charitable features, is essentially an insurance corporation conducted on the assessment plan, and cannot escape liability for torts of its agents on the theory that it is a charitable corporation. Morse v. Modern Woodmen of America, 166 Wis. 194, Ann. Cas. 1918 D 480, 164 N. W. 829.

⁷¹ A local Y. M. C. A. is liable

for injuries, in an elevator accident, to a student who had paid tuition equal to charges for like schooling in other schools operated for profit, it not being shown that the Y. M. C. A. was a charitable corporation. Susman v. Y. M. C. A. of Seattle, 101 Wash. 487, 172 Pac. 554.

⁷² A railroad company is not exempt on the theory of charitable corporation, for negligence of its employee in charge of an emergency hospital supported by the railroad. Fontanella v. New York Cent. R. Co., 186 N. Y. App. Div. 588, 174 N. Y. Supp. 537.

⁷³ See *infra*, this section.

Cornell University, as a charitable corporation, is not liable to a student injured by an explosion while performing an experiment under the directions of an instructor. Hamburger v. Cornell University, 99 N. Y. Misc. 564, 166 N. Y. Supp. 46.

⁷⁴ See *infra*, this section.

or liability because of contract.⁷⁵ Thus, a charitable hospital is not liable in damages for the failure of its medical superintendent to comply with a contract made by him for the care of a patient being treated in the hospital.⁷⁶ It has been held in New York, however, that if there is a contract by a charitable hospital to care for a child while the mother is undergoing treatment in the hospital, the hospital is liable for a breach of the contract in permitting the child to come in contact with a hot steam pipe.⁷⁷ So in Tennessee, Vanderbilt University, although a charitable corporation, was held liable, to the extent of income derived from an office building operated largely for profit, for death of a tenant in an elevator accident due to negligence.⁷⁸

In Texas, a charitable hospital corporation is liable to a servant for negligence.⁷⁹ And in New York a hospital, although public, is liable to strangers other than patients for torts of its employees in the scope of their duty.⁸⁰ So, in New York, a charitable hospital is liable for negligently running over a person while answering a city police call, especially where paid therefor by the city.⁸¹ In Oregon, an Odd Fellows Home, organized under a statute limiting the use of its resources to charitable objects, is not liable for injuries to a laundress working therein.⁸²

The mere fact that a charitable corporation takes out an indemnity policy for an elevator does not create liability for torts of the elevator operator.⁸³

In regard to the liability of a charitable corporation for a tort, federal courts will follow the law of the state where the corporation was created and supported, although plaintiff is a non-resident.⁸⁴

⁷⁵ *Roosen v. Peter Bent Brigham Hospital*, — Mass. —, 126 N. E. 392.

⁷⁶ *Davin v. Kansas Medical Missionary Ass'n*, 103 Kan. 48, 172 Pac. 1002.

⁷⁷ *Roche v. St. John's Riverside Hospital*, 96 N. Y. Misc. 289, 160 N. Y. Supp. 401.

⁷⁸ *Gamble v. Vanderbilt University*, — Tenn. —, 200 S. W. 510.

⁷⁹ *Hotel Dieu v. Armendarez*, — Tex. —, 210 S. W. 518.

⁸⁰ *Murtha v. New York Homeopathic Medical College & Flower*

Hospital, 228 N. Y. 183, 126 N. E. 722, aff'g 183 N. Y. App. Div. 886, 169 N. Y. Supp. 1105.

⁸¹ *Van Ingen v. Jewish Hospital of Brooklyn*, 99 N. Y. Misc. 655, 164 N. Y. Supp. 832, holding exemption from liability extends only to beneficiaries or patients.

⁸² *O'Neill v. Odd Fellows Home*, 89 Ore. 382, 174 Pac. 148.

⁸³ *Susman v. Y. M. C. A.*, 101 Wash. 487, 172 Pac. 554.

⁸⁴ *Paterlini v. Memorial Hospital Ass'n*, 247 Fed. 639.

CHAPTER 53

CRIMES AND PENALTIES

- § 3364. In general.
- § 3365. Corporation as "person," etc., within criminal statute.
- § 3367. Unauthorized and ultra vires acts.
- § 3368. Crimes with basis in misfeasance.
- § 3369. Crimes involving malice or intent.
- § 3370. Crimes involving personal violence.
- § 3371. Nuisances.
- § 3374. Miscellaneous crimes.
- § 3375. Instituting prosecution.

§ 3364. In general. In Indiana, where there are no common-law crimes, corporations may be indicted only when the legislature has specifically so provided.¹ In Texas it is said that "there is no provision of law in this state under which a firm or corporation can be indicted or tried under the criminal laws."² In most states, however, a corporation is liable to indictment or other criminal process.³ It seems that a corporation as such cannot be criminally libeled.⁴

§ 3365. Corporation as "person," etc., within criminal statute.⁵ The Texas statute penalizing "any person" carrying on certain business without a license does not apply to corporations.⁶ The word "whoever" in the Espionage Act providing punish-

¹ State v. Terre Haute Brewing Co., 186 Ind. 248, 115 N. E. 772.

² Judge Lynch International Book & Publishing Co. v. State, 84 Tex. Cr. App. 459, 208 S. W. 526.

³ Postal Telegraph-Cable Co. v. City of Charlottesville, — Va. —, 101 S. E. 357.

A corporation is subject to prosecution by information for

the violation of a penal statute, and may be fined. People v. Saline County Coal Co., 206 Ill. App. 266.

⁴ Potter v. State, — Tex. Cr. App. —, 216 S. W. 886.

⁵ See also § 54, supra.

⁶ Judge Lynch International Book & Publishing Co. v. State, 84 Tex. Cr. App. 459, 208 S. W. 526.

ment for "whoever" wilfully obstructs recruiting or enlistment service in time of war, includes corporations.⁷

§ 3367. Unauthorized and ultra vires acts. Where a corporation claims that the act charged was contrary to its will and direction, other acts of a like character may be shown in evidence as bearing on authorization of the corporate agent.⁸

§ 3368. Crimes with basis in misfeasance. Liability extends to acts of malfeasance as well as nonfeasance.⁹ It "has long been settled in this state that a corporation aggregate may in a proper case be held criminally for acts of malfeasance as well as for nonfeasance."¹⁰

§ 3369. Crimes involving malice or intent. A corporation may be criminally liable even though the act involves specific intent.¹¹ Thus, a publishing company is responsible for the acts of its agents in printing and publishing a pamphlet containing statements tending to cause insubordination in the military service, in violation of the Espionage Act.¹²

§ 3370. Crimes involving personal violence. A corporation may be guilty of manslaughter.¹³

§ 3371. Nuisances. A corporation is not criminally liable for a nuisance, where not negligent and not acting beyond its corporate powers.¹⁴

⁷ United States v. American Socialist Society, 260 Fed. 885.

⁸ People v. Title Guaranty & Trust Co., 180 N. Y. App. Div. 648, 168 N. Y. Supp. 278.

⁹ United States v. Nearing, 252 Fed. 223, 231.

¹⁰ State v. Lehigh Valley R. Co., 90 N. J. L. 372, 103 Atl. 685.

¹¹ United States v. Nearing, 252 Fed. 223, 231.

A corporation may be guilty of a specific intent, although such in-

tent involves an evil purpose to do a wrongful act. United States v. American Socialist Society, 260 Fed. 885.

¹² United States v. Nearing, 252 Fed. 223, 231.

¹³ State v. Lehigh Valley R. Co., 92 N. J. L. 261, 106 Atl. 23; State v. Lehigh Valley R. Co., 90 N. J. L. 372, 103 Atl. 685.

¹⁴ State v. Riggs, 92 N. J. L. 571, 106 Atl. 216, street railway erecting poles and stringing wires.

§ 3374. Miscellaneous crimes.¹⁵ A corporation may be prosecuted for violation of the Espionage Act.¹⁶

The federal statute making it a crime for corporations to make contributions in connection with elections for congressmen is constitutional.¹⁷ The Indiana statute making a crime contributions, etc., by any private corporation "to promote the success or defeat of any candidate for public office or of any political party or principle or for any other political purpose whatever" does not apply to a contribution by a brewing company to promote the success of a principle at a local option election.¹⁸

§ 3375. Instituting prosecution. If the injured party is a corporation, an indictment should so state.¹⁹ An erroneous allegation in an indictment for burglary that the owner of the building was a corporation is immaterial.²⁰

¹⁵ Practicing law, see § 820, *supra*.

¹⁶ *United States v. American Socialist Society*, 260 Fed. 885.

Where the author of a book and the corporation which published and distributed it are joined as defendants in a prosecution under the Espionage Act for obstructing recruiting service, the corporation may be found guilty, although the author is ac-

quitted. *United States v. American Socialist Society*, 260 Fed. 885.

¹⁷ *United States v. United States Brewing Ass'n*, 239 Fed. 163.

¹⁸ *State v. Terre Haute Brewing Co.*, 186 Ind. 248, 115 N. E. 772.

¹⁹ *Whitaker v. State*, 85 Tex. Cr. App. 272, 211 S. W. 787.

²⁰ *Long v. State*, 140 Ark. 413, 216 S. W. 306.

CHAPTER 54

MONOPOLIES AND TRUSTS

- § 3388. Constitutionality of anti-trust statutes—State statutes.
- § 3389. Interstate trade and commerce considered.
- § 3390. Monopolization under anti-trust statutes.
- § 3391. Restraint of trade.
- § 3393. Motive, intent and result.
- § 3394. Means of accomplishing violation of anti-trust statutes.
- § 3395. Patents.
- § 3397. Criminal prosecutions.
- § 3399. Relief awarded government.
- § 3400. Actions for treble damages—In general.
- § 3401. — Persons who may sue and be sued; venue; limitations; pleading, etc.
- § 3402. Violation of anti-trust statute as defenses to action.

§ 3388. Constitutionality of anti-trust statutes—State statutes. The 1916 anti-trust statute of Kentucky is void because exempting from its operation nonstock companies and those not engaged in mining, manufacturing or transportation; but anti-trust statutes do not deny the equal protection of the law to corporations merely because the penalty for violation by corporations is a fine not exceeding ten thousand dollars and forfeiture of charter while the maximum penalty which may be inflicted on an individual is five thousand dollars.¹

§ 3389. Interstate trade and commerce considered. Contracts made by an advertising agency for the insertion of advertising in periodicals does not constitute commerce within the Sherman Act, although the circulation and distribution of such periodicals amounts to interstate commerce.² While the ownership by a railroad of stock of a mining company does not necessarily create an identity of corporate interest between the two such as to render

¹ *Com. v. Hatfield Coal Co.*, 186 Ky. 411, 217 S. W. 125. *ing Agency v. Curtis Pub. Co.*, 252 U. S. 436, 64 L. Ed. 649.

² *Blumenstock Bros. Advertis-*

it unlawful under the federal commodities clause for the railroad to transport in interstate commerce the products of such mining company, yet where such ownership of stock is resorted to, for the purpose of making the mining company a mere agent or instrumentality or department, courts will look through the forms to the realities of the relation between the companies as if the corporate agency did not exist and will deal with them as the justice of the case may require.³

§ 3390. Monopolization under anti-trust statutes.⁴ The United States Steel Corporation is not a monopoly, so as to require its dissolution, for the reason that competition was not restrained; and neither the size of the corporation and its potency for mischief nor the fact that competitors voluntarily follow its prices is ground for its dissolution as a violation of the Sherman Act.⁵ The United Shoe Machinery Company, composed of several non-competing companies, is not a monopoly so as to be within the federal anti-trust act, because of its method of leasing patented machines.⁶ A failing concern may, without violating the Sherman Anti-trust Act, sell its plant to its only competitor, instead of disposing of it as junk.⁷

A reorganization of the Reading railroad and a large coal company, whereby a holding company acquired all the stock of the two, was a violation of the federal statutes as a "combination

³ United States v. Reading Co., 253 U. S. 26, 64 L. Ed. 760, rev'g in part 226 Fed. 229.

⁴ Combination of foreign owners of steamship lines to end competition held violation of Sherman Act, see Thomsen v. Cayser, 243 U. S. 66, 61 L. Ed. 597, rev'g Union Castle Mail S. S. Co. v. Thomsen, 190 Fed. 536.

Combination of three pulpwood supply agencies as monopoly, see Pulpwood Co. v. Green Bay Paper & Fiber Co., 168 Wis. 400, 170 N. W. 230.

Fish companies as monopoly, see United States v. New England Fish Exchange, 258 Fed. 732.

Combinations to prevent com-

petition, see United States v. American Column & Lumber Co., 263 Fed. 147.

⁵ United States v. United States Steel Corporation, 251 U. S. 417, 64 L. Ed. 343, 8 A. L. R. 1121, aff'g 223 Fed. 55.

⁶ United States v. United Shoe Machinery Co. of New Jersey, 247 U. S. 32, 62 L. Ed. 968, aff'g 222 Fed. 349.

The United Shoe Machinery Company was held guilty of violating the Clayton Act in the making of leases of machines in United States v. United Shoe Machinery Co., 264 Fed. 138.

⁷ American Press Ass'n v. United States, 245 Fed. 91.

to unduly restrain interstate commerce.”⁸ Consolidation of New York Central, Michigan Central, and Lake Shore railroads did not violate the federal anti-trust law, where the former already owned ninety per cent of the stock of the other companies.⁹ A purchase by a lessee railroad of the stock of the lessor road is not a violation of the Sherman Act where, from the time of their construction, there had been no competition between them because of a continuous common control.¹⁰

The business of furnishing abstracts of title is not susceptible of monopoly in the sense in which the business of dealing in a commercial product may be monopolized.¹¹ The Washington Constitution, in so far as it forbids combination of corporations “for the purpose of fixing the price or limiting the production,” does not apply where one of three competing abstract companies bought out one of its competitors and took a lease of the plant of the other, to prevent ruinous competition.¹²

The appointment by an Ohio company of a New York company as its exclusive selling agent is not violative of the common law nor the Sherman Act.¹³ A covenant by a selling corporation not to engage in the same business within a certain area and within a reasonable time does not create a monopoly.¹⁴ Ownership by one company of a majority of the stock of another does not, of course, necessarily lessen competition between them nor create a monopoly.¹⁵

§ 3391. Restraint of trade.¹⁶ Where a manufacturing company enters into agreements—whether express or implied from

⁸ *United States v. Reading Co.*, 253 U. S. 26, 64 L. Ed. 760, rev'g in part 226 Fed. 229.

⁹ *Venner v. New York Cent. & H. River R. Co.*, 177 N. Y. App. Div. 296, 164 N. Y. Supp. 626.

¹⁰ *United States v. Southern Pac. Co.*, 239 Fed. 998.

¹¹ *Lumbermen's Trust Co. v. Title Ins. & Inv. Co. of Tacoma*, 248 Fed. 212.

¹² *Lumbermen's Trust Co. v. Title Ins. & Inv. Co. of Tacoma*, 248 Fed. 212.

¹³ *Baran v. Goodyear Tire & Rubber Co.*, 256 Fed. 571.

¹⁴ *Lumbermen's Trust Co. v. Title Ins. & Inv. Co. of Tacoma*, 248 Fed. 212.

¹⁵ *Niles-Bement-Pond Co. v. Iron Molders' Union*, 246 Fed. 851.

¹⁶ Contract to sell stock in old bank to prevent establishment of a new bank as an illegal combination to prevent the establishment of a new bank, see *Edwards v. Roberts*, — Tex. Civ. App. —, 222 S. W. 278.

Unfair competition, under Oklahoma anti-trust statute, see *Western Lumber Co. v. State*, — Okla. —, 189 Pac. 868.

a course of dealing or other circumstances—with all customers throughout the several states, which bind them to observe fixed resale prices, there is a combination in restraint of trade in violation of the Sherman Act.¹⁷ But a manufacturing company, where it has no intent to create or maintain a monopoly, does not violate the Sherman Act by refusing to deal with those who do not conform to resale prices fixed by it.¹⁸ A refusal of a tire manufacturer to sell to dealers (a) who will not maintain suggested prices or (b) will sell to other dealers and not merely to the consumer, is not a violation of the Sherman Act.¹⁹

Reading Company, owning Reading railroad and large coal mines, which afterwards purchased another railroad to prevent competition in sale of anthracite coal, was a combination in restraint of trade so as to be subject to dissolution under the federal statutes.²⁰

A purchase by one insurance company of all the assets of another does not violate the Texas anti-trust statute unless made for the purpose of preventing or lessening competition or it has such effect.²¹

§ 3393. Motive, intent and result.²²

§ 3394. Means of accomplishing violation of anti-trust statutes. The necessary unlawful agreement to constitute a com-

¹⁷United States v. A. Schraeder's Son, Inc., 252 U. S. 85, 64 L. Ed. 471, rev'g 264 Fed. 175, and distinguishing United States v. Colgate & Co., 250 U. S. 300, 63 L. Ed. 992, on the ground that in the latter case the manufacturer merely indicated his wish regarding resale prices and refusal to deal with all who failed to observe them. To same effect, see Ford Motor Co. v. Union Motor Sales Co., 244 Fed. 156.

¹⁸United States v. Colgate & Co., 250 U. S. 300, 63 L. Ed. 992, aff'g 253 Fed. 522.

Agreement between manufacturer and customer as to resale

price, and refusal to sell to customers who refuse to agree to abide by the resale price, is not a combination in restraint of trade under the Sherman Anti-Trust Act. United States v. Colgate & Co., 253 Fed. 522.

¹⁹Baran v. Goodyear Tire & Rubber Co., 256 Fed. 571.

²⁰United States v. Reading Co., 253 U. S. 26, 64 L. Ed. 760, rev'g in part 226 Fed. 229.

²¹California State Life Ins. Co. v. Kring, — Tex. Civ. App. —, 208 S. W. 372.

²²Presumption as to intent, see Bluefields S. S. Co. v. United Fruit Co., 243 Fed. 1, 14.

bination or conspiracy in violation of the Sherman Act may be tacit as well as expressed.²³

§ 3395. Patents. The exertion of the right given a patentee to exclude others from the use of his invention, absolutely or upon terms, is not an offense against the federal anti-trust act.²⁴ Prohibitions against restraint of trade apply to patented as well as unpatented articles.²⁵

§ 3397. Criminal prosecutions. Under the North Dakota anti-trust statutes the common-law remedy of quo warranto to dissolve a corporation is not superseded by a criminal remedy or another civil remedy, and the civil remedy is not conditioned on a successful criminal prosecution.²⁶

§ 3399. Relief awarded government. Whether a dissolution of the corporation shall be decreed rests in the discretion of the court, due consideration being given to the facts that the unlawful acts have ceased and the interests of the public.²⁷

§ 3400. Actions for treble damages—In general.²⁸ Actions for treble damages must be based on a substantial cause of action.²⁹ A cause of action to recover triple damages under the Sherman Act is not assignable and does not pass to the plaintiff's trustee in bankruptcy.³⁰ It does not survive the death of the person injured.³¹ In an earlier federal case, however, it was held that the action survives the death of the person or dissolution of a corporation injured.³²

²³ United States v. M. Piowaty & Sons, 251 Fed. 375.

²⁴ United States v. United Shoe Machinery Co. of New Jersey, 247 U. S. 32, 62 L. Ed. 968, aff'g 222 Fed. 349, quoted from at length on pp. 5500, 5501.

²⁵ United States v. A. Schraeder's Son, Inc., 264 Fed. 175; United States v. United Shoe Machinery Co., 264 Fed. 138.

²⁶ State ex rel. Langer v. Gamble-Robinson Fruit Co., — N. D. — 176 N. W. 103.

²⁷ United States v. American Can Co., 234 Fed. 1019.

²⁸ See Buckeye Powder Co. v. E. I. Du Pont de Nemours Powder Co., 248 U. S. 55, 63 L. Ed. 123, aff'g 223 Fed. 881.

²⁹ Blumenstock Bros. Advertising Agency v. Curtis Pub. Co., 252 U. S. 436, 64 L. Ed. 649.

³⁰ Bonvillain v. American Sugar Refinery Co., 250 Fed. 641.

³¹ Caillouet v. American Sugar Refining Co., 250 Fed. 639.

³² Imperial Film Exchange v. General Film Co., 244 Fed. 985.

§ 3401. — Persons who may sue and be sued; venue; limitations; pleading, etc. The fact that a cause of action is based on the Sherman Law does not give to individual stockholders the right to interfere with the internal management of the corporation nor, in any case, to resort to an action at law instead of a suit in equity.³³ Where plaintiff corporation participated in the unlawful combination in restraint of trade by virtue of defendant acquiring a controlling interest in its stock, it cannot recover damages under the Sherman Act for injuries from the combination.³⁴

Courts have jurisdiction, under the Clayton Act, in any district where a corporation transacts business, whether it is "found" there or not.³⁵ A corporation is "found" within a district, so as to be suable within the Sherman Act, where it has an office and does business.³⁶ The words "resides or is found," in the Sherman Act, means that the corporation must be present in the district, by its officers or agents, carrying on its business.³⁷

§ 3402. Violation of anti-trust statute as defense to action. A stockholder who has voluntarily become a part of a corporation operating in violation of a state anti-trust statute cannot obtain relief against the corporation or other stockholders, where himself a party to the illegal acts.³⁸ Where a sale of its property by one company to another has been consummated in violation of an anti-trust statute, a maker of a note acquired by the purchaser cannot set up the anti-trust statute as a defense.³⁹

³³ *United Copper Securities Co. v. Amalgamated Copper Co.*, 244 U. S. 261, 61 L. Ed. 1119, aff'g 223 Fed. 421.

³⁴ *Bluefields S. S. Co. v. United Fruit Co.*, 243 Fed. 1.

³⁵ *Southern Photo Material Co. v. Eastman Kodak Co.*, 234 Fed. 955.

³⁶ *Venner v. Pennsylvania Steel Co.*, 250 Fed. 292.

³⁷ *People's Tobacco Co. v. American Tobacco Co.*, 246 U. S. 79, 62 L. Ed. 587.

³⁸ *Duane v. Merchants' Legal Stamp Co.*, 231 Mass. 113, 120 N. E. 370.

³⁹ *California State Life Ins. Co. v. Kring*, — Tex. Civ. App. —, 208 S. W. 372.

CHAPTER 55

CONTEMPT

§ 3408. Liability of officers, agents, directors, etc.

§ 3408. Liability of officers, agents, directors, etc. Directors who pass a resolution authorizing the filing of a voluntary petition in bankruptcy, as well as officers who execute such a petition, are guilty of contempt in violating an injunction restraining exercise of any of the corporate privileges and franchises.¹ Advice of counsel is no excuse for violation of an injunction by directors.²

¹ Cavagnaro v. Indian Tire & Rubber Co., 90 N. J. Eq. 532, 107 Atl. 643.

² Cavagnaro v. Indian Tire & Rubber Co., 90 N. J. Eq. 532, 107 Atl. 643.

CHAPTER 56

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- § 4283. Members as partners inter se.

I. GENERAL CONSIDERATIONS

§ 3413. Capital stock. The term “capital stock” means “the fund, property, or other means contributed or agreed to be contributed by shareholders as the financial basis for the prosecu-

tion of the business of the corporation, being made directly through stock subscriptions or indirectly through the declaration of stock dividends.”¹ “Capital stock,” as the term is used in a statute making directors liable to the amount of the “capital stock so divided, withdrawn, paid out, or reduced,” means “not the shares of which the nominal capital is composed, but the actual capital, i. e., assets, with which the corporation carries on its corporate business.”² The term “capital stock” does not designate the shares of stock owned by the shareholder, either separately or in the aggregate, or the identical lands, chattels, or other articles of property owned by the corporation, but it does designate the aggregate property of the corporation, not in separate parcels, but as homogeneous unit.³

§ 3414. Capital. Capital means the actual property or estate of the corporation, whether in money or property.⁴ Capital stock is distinguishable from capital.⁵

§ 3415. Stock. “Actual book value” of national bank stock is the corporate assets minus the liabilities and other matters required to be deducted.⁶

§ 3417. Shares of stock. Shares of stock may be the subject of a trust agreement.⁷ Such a trust is governed by the same rules governing all trusts.⁸

¹Dodge v. Ford Motor Co., 204 Mich. 459, 170 N. W. 668.

Other definitions, see United States v. New York, N. H. & H. R. Co., 265 Fed. 331; Central Illinois Public Service Co. v. Swartz, 284 Ill. 108, 119 N. E. 990; Turner v. Cattlemen's Trust Co., — Tex. —, 215 S. W. 831, and see § 3455, *infra*.

Definition of “paid-up capital stock,” see Boston & M. R. R. v. United States, 265 Fed. 578; United States v. New York, N. H. & H. R. Co., 265 Fed. 331.

²Merchants' & Insurers' Reporting Co. v. Schroeder, 39 Cal. App. 226, 178 Pac. 540.

³Central Illinois Public Service Co. v. Swartz, 284 Ill. 108, 119 N. E. 990.

⁴See Turner v. Cattlemen's Trust Co., — Tex. —, 215 S. W. 831.

⁵In re Caledonia Coal Co., 254 Fed. 742, 746.

⁶Gurley v. Woodbury, 177 N. C. 70, 97 S. E. 754. Compare Lane v. Barnard, 185 N. Y. App. Div. 754, 173 N. Y. Supp. 714.

⁷See Crosby v. Robbins, 56 Mont. 179, 182 Pac. 122.

⁸See Carter v. Bugbee, 92 N. J. L. 390, 106 Atl. 412.

§ 3418. Distinction between capital stock and shares of stock. Capital or capital stock is not the same thing as shares of capital stock.⁹ Shares of stock are a distinct entity from the capital stock or property and assets of the corporation.¹⁰

§ 3421. Treasury stock. Where stock was fully issued and not a new issue or a reissue to subscribers, it was not treasury stock.¹¹

§ 3423. Shareholders and stockholders. A person in possession of stock and exercising acts of ownership over it is presumed to be the owner.¹² A presumption of ownership of stock from the possession of a certificate of stock indorsed in blank is overcome by showing that the possessor never had the stock transferred to himself on the books and that during all the time he had the stock in his possession he permitted the former owner to vote the stock, draw the dividends, and enjoy all the privileges and benefits of an owner.¹³ Ownership of stock shown once to exist is not, it seems, presumed to continue.¹⁴ Even where legal title to stock is vested in a certain person, equity will treat him as a trustee holding it for its real and beneficial owners, in a proper case.¹⁵ A party to a proposed reorganization afterwards repudiated is not a stockholder, especially where he stopped payment on his check given for stock in the proposed reorganization.¹⁶ Where the corporate assets are sold under an agreement between the stockholders as to how the proceeds should be divided among them, such agreement governs the distribution rather than prior contracts made at the time of incorporation.¹⁷

Where the United States asserts as a stockholder any rights

⁹ First Nat. Bank of Cincinnati, Ohio v. Durr, 246 Fed. 163.

¹⁰ State v. First Nat. Bank of Aurora, 103 Neb. 280, 171 N. W. 912.

¹¹ Rochelle Roofing Co. v. Burley & Stevens, 226 Mass. 349, 115 N. E. 478, stock issued to president and held by him in trust.

¹² Bumiller v. Bumiller, 179 Cal. 119, 175 Pac. 897; Cooper v. Eastern Horse & Mule Co., — Del. Ch. —, 110 Atl. 666.

¹³ Stoltz v. Carroll, 99 Ohio St. 289, 124 N. E. 226.

¹⁴ Wilkinson v. Grant, — Cal. App. —, 189 Pac. 319.

¹⁵ Clayton v. Smith, 131 Md. 562, 102 Atl. 925.

¹⁶ Elkhorn By-Product Coal Co. v. Tynes, 188 Ky. 269, 221 S. W. 514.

¹⁷ Meierhoffer v. Kennedy, — Mo. App. —, 223 S. W. 624.

with respect to the conduct of the affairs of the corporation, its contracts or its torts, the federal rights, duties and privileges are no greater than those of any other stockholder.¹⁸

II. CERTIFICATES OF STOCK

§ 3424. Definition and nature.¹⁹

§ 3425. **Certificate is not the stock itself.** Certificates of stock are not themselves stock nor do they constitute title to stock, but they are merely evidence of title.²⁰

§ 3426. **Certificate of stock as property.** In replevin for shares of stock, the complaint must identify the certificates sued for.²¹

§ 3427. **Necessity for issue of certificates.** A certificate need not issue to effectuate an issue of stock,²² nor to constitute one a stockholder.²³

III. SHARES OF STOCK AS PROPERTY

§ 3429. **General rule.** Shares of stock are property within the protection afforded to property by federal and state constitutions.²⁴ Shares of stock, even in a mining company, are personal property.²⁵ A charter provision that the stock of land companies shall be deemed personal property does not make the interest of the stockholders in lots acquired from the corporation personal rather than real property, simply because the ownership of such

¹⁸ Chesapeake & Delaware Canal Co. v. United States of America, 250 U. S. 123, 63 L. Ed. 888, aff'g 240 Fed. 903.

¹⁹ Other definitions, see Malley v. Bowditch, 259 Fed. 809.

²⁰ Atkins v. Garrett, 252 Fed. 280; Brumbaugh v. Mellinger, — Ind. App. —, 120 N. E. 676.

²¹ Lamus v. Engwicht, 39 Cal. App. 523, 179 Pac. 435.

Necessary parties in replevin to recover stock, see Lutz v. Mer-

chants' Nat. Bank of San Diego, 179 Cal. 401, 177 Pac. 158.

²² Fidelity Trust Co. v. Federal Trust Co., 87 N. J. Eq. 550, 100 Atl. 615.

²³ Williams v. Everett, — Mo. —, 200 S. W. 1045; Lask v. Bedell, — N. J. Eq. —, 109 Atl. 849.

²⁴ Duane v. Merchants' Legal Stamp Co., 231 Mass. 113, 120 N. E. 370.

²⁵ Page v. Walser, 43 Nev. 422, 187 Pac. 509.

lots is attached to the ownership of such stock.²⁶ Shares of stock may be the subject of an attorney's lien, where the fruits of a judgment obtained by him.²⁷

§ 3430. Are incorporeal and intangible property. An action does not lie to quiet title to shares of stock.²⁸

§ 3431. Shares of stock as "choses in action," "credits," "debts," "money," or "securities."²⁹

§ 3434. Situs of shares of stock. The situs of shares of stock ordinarily is at the domicile of the corporation.³⁰ Corporate stock is property, whatever its value may be, and its situs is in the state where the corporation was created, where its ownership is in question.³¹ Likewise, for jurisdictional purposes, the situs is in the state where the corporation was created.³² An action to determine title to stock is one quasi in rem, and the physical presence of the certificates within the jurisdiction does not make the action one in personam.³³

IV. LIABILITY OF SHARES OF STOCK TO EXECUTION, ATTACHMENT AND GARNISHMENT

§ 3437. Statutory authority. In Oklahoma, by statute, shares of stock are attachable.³⁴ In some states, statutes permitting levies on stock do not apply to stock of a foreign corporation.³⁵

²⁶ *In re Berry*, 247 Fed. 700, 707.

²⁷ *Clark v. O'Donnell*, — Colo. —, 187 Pac. 534.

²⁸ *Lamus v. Engwicht*, 39 Cal. App. 523, 179 Pac. 435.

²⁹ Shares of stock as "interest bearing securities," see *Williams v. Cobb*, 242 U. S. 307, 61 L. Ed. 325, aff'g 219 Fed. 663.

³⁰ *Hudson Nav. Co. v. Murray*, 236 Fed. 419; *Warner v. Brown*, 231 Mass. 338, 121 N. E. 69; *Troll v. Third Nat. Bank of St. Louis*, — Mo. —, 216 S. W. 922; *Le Roy Sargent & Co. v. McHarg*, — S. D. —, 174 N. W. 742, and see § 3439, *infra*.

³¹ *Le Roy Sargent & Co. v.*

McHarg, — S. D. —, 174 N. W. 742, citing *Fletcher Cyc. Corp.* § 3434.

³² *Le Roy Sargent & Co. v. McHarg*, — S. D. —, 174 N. W. 742.

In Colorado, however, it is held that the situs, for jurisdictional purposes, of shares of stock, is where the certificates are. *Clark v. O'Donnell*, — Colo. —, 187 Pac. 534.

³³ *Hudson Nav. Co. v. Murray*, 236 Fed. 419.

³⁴ *Harris v. Mid-Continent Life Ins. Co.*, 75 Okla. 105, 182 Pac. 85.

³⁵ *Mitchell v. Leland Co.*, 246 Fed. 103, Washington statute.

§ 3439. Situs of stock. The situs of shares of stock, for purposes of levy, is where the corporation resides, although the stock is owned by a nonresident.³⁶ Certificates of stock are personal property, within the Washington statute, so as to be subject to levy and sale, if physically within the state, provided the levy and sale are made in pursuance of the statute.³⁷

§ 3440. Title.³⁸ Stock already transferred cannot be levied on as the stock of the transferor.³⁹ Shares of stock standing in the name of the debtor are not subject to execution, against him where they were previously assigned to another.⁴⁰ A claimant of shares of stock levied on has the burden of proving ownership prior to the rendition of the judgment on which was based the execution levied thereon.⁴¹

§ 3442. Persons in whose hands stock may be levied upon. Stock belonging to a stockholder may be levied on in the hands of the corporation.⁴² It may be attached, in the hands of the corporation, in Oklahoma, but the certificates of stock cannot be attached in the hands of the stockholder.⁴³

§ 3443. Mode of levy and sale.⁴⁴ Claimants to stock levied on may, but are not required to, become parties to the attachment suit, under the Pennsylvania statutes.⁴⁵ In West Virginia, shares of stock cannot be "sold" on execution.⁴⁶

³⁶ Stock owned by a nonresident may be levied on at the domicile of the corporation. *Harris v. Mid-Continent Life Ins. Co.*, 75 Okla. 105, 182 Pac. 85.

³⁷ *Mitchell v. Leland Co.*, 246 Fed. 103.

³⁸ Effect of unregistered transfer, see § 3811, *infra*.

³⁹ *Duquesne Bond Corporation v. American Surety Co. of New York*, 264 Pa. 203, 107 Atl. 759.

⁴⁰ *Allen v. Williams*, 212 Ill. App. 114.

⁴¹ *Tompkins v. American Land Co.*, — Ga. App. —, 103 S. E. 190.

⁴² *Turner v. Cattlemen's Trust Co.*, — Tex. —, 215 S. W. 831.

⁴³ *Harris v. Mid-Continent Life Ins. Co.*, 75 Okla. 105, 182 Pac. 85.

⁴⁴ Statutory method of levying on shares of stock, see *Tompkins v. American Land Co.*, — Ga. App. —, 103 S. E. 190.

Method of procedure in West Virginia, after shares of stock have been levied on, see *Lambert v. Huff, Andrews & Thomas Co.*, 82 W. Va. 362, 1 A. L. R. 650, 95 S. E. 1031.

⁴⁵ *Duquesne Bond Corporation v. American Surety Co. of New York*, 264 Pa. 203, 107 Atl. 759.

⁴⁶ *Lambert v. Huff, Andrews & Thomas Co.*, 82 W. Va. 362, 1 A. L. R. 650, 95 S. E. 1031.

§ 3444. **Effect of levy and sale.**⁴⁷ A purchaser of corporate stock at execution sale does not take absolute title, in case of a mutual water corporation not organized for profit but merely to supply water to stockholders.^{47a}

V. CONVERSION OF SHARES OF STOCK

§ 3448. **What constitutes a conversion—Conversion by third person.** Failure of an agent to deliver stock bought for his principal is a conversion.⁴⁸ A sale by brokers of stock put up as margin, without giving notice as agreed on, is a conversion of the stock.⁴⁹ One who borrows stock to use as collateral and who converts it by attempting to transfer it absolutely, is liable in damages to the owner.⁵⁰ Failure to pay the stamp tax on transfers of stock does not bar an action for conversion against a custodian.⁵¹ An election to recover the stock itself wrongfully withheld bars the right to sue for the value of the stock converted.⁵²

§ 3449. **Measure of damages—General rules.** In New York, the value of the stock at the time it was converted, i. e., when a demand was made for it, and not at the time of the delivery of the stock to the person converting it, is the measure of damages.⁵³

§ 3451. — **Method of estimating value.** For converting stock having no market value, there may be considered the value of the corporate assets, the amount of liabilities, and the earning power for a number of years prior to the conversion.⁵⁴

⁴⁷ Levy as precluding right to transfer stock, see § 3823, *infra*.

Garnishment of corporate stock as covering subsequently declared dividends, see generally *Savings Bank of Danbury v. Loewe*, 242 U. S. 357, 61 L. Ed. 360, *aff'g* 236 Fed. 444.

^{47a} *Woodstone Marble & Tile Co. v. Dunsmore Canyon Water Co.*, — Cal. App. —, 190 Pac. 213.

⁴⁸ *Mundheim v. C. A. Bertrand & Co.*, — N. Y. Misc. —, 180 N. Y. Supp. 871.

⁴⁹ *White v. Slayback*, 189 N. Y. App. Div. 564, 178 N. Y. Supp.

421. See also *O'Connor v. Graff*, 186 N. Y. App. Div. 116, 173 N. Y. Supp. 730.

⁵⁰ *Crosby v. Simpson*, — Mass. —, 125 N. E. 616.

⁵¹ *Noble v. Haff*, — N. Y. Misc. —, 172 N. Y. Supp. 139.

⁵² *White Star Coal Co. v. Pursi-*
full, 189 Ky. 296, 224 S. W. 858.

⁵³ *Noble v. Haff*, — N. Y. Misc. —, 172 N. Y. Supp. 139.

⁵⁴ *Gorham v. Massillon Iron & Steel Co.*, 284 Ill. 594, 120 N. E. 467, *aff'g* 209 Ill. App. 606, 616, 618.

§ 3453. — **Nominal damages.** In case of conversion of stock by the corporation by refusal to issue certificates, plaintiff is entitled to at least nominal damages.⁵⁵

VI. AMOUNT OF CAPITAL STOCK AND INCREASE AND REDUCTION THEREOF

§ 3455. **Amount of original capital stock.** Profits and undeclared dividends used by a corporation in its business are not "capital stock" within the Michigan statute limiting the amount of "capital stock" of manufacturing corporations to a certain sum.⁵⁶ Where a statute provided that no bank should be incorporated with less than a specified amount of capital stock, a bank could fix a minimum capital stock greater than that specified in the statute; and where only one amount is named such amount is both the maximum and the minimum.⁵⁷

§ 3456. **Par value of shares and shares without expressed par or nominal value.**⁵⁸ Holders of stock having no par value are liable to creditors just as they would be if the shares had a par value.⁵⁹

§ 3458. **Increase of original or authorized capital stock—Power and authority to make increase.** The charter may be amended so as to increase the capital stock, although a prior amendment had limited the amount of capital stock.⁶⁰ The certificate of the secretary of state that the capital stock of a company was increased a certain sum is not conclusive of the legality of the increase as against a judgment creditor.⁶¹

⁵⁵ *Boglin v. Earl-Eagle Min. Co.*, — Utah —, 184 Pac. 190.

⁵⁶ *Dodge v. Ford Motor Co.*, 204 Mich. 459, 170 N. W. 668. In 1917 the maximum of capital stock was doubled by fixing it at fifty million.

⁵⁷ *Smith v. Citizens' & Southern Bank*, 148 Ga. 764, 98 S. E. 466.

⁵⁸ Non-par stock, article on, see 90 Cent. L. J. 170-177.

⁵⁹ *State ex rel. Standard Tank Car Co. v. Sullivan*, — Mo. —, 221 S. W. 728, citing *Fletcher Cyc. Corp.*

⁶⁰ *Venner v. American Telephone & Telegraph Co.*, 110 N. Y. Misc. 118, 181 N. Y. Supp. 45.

⁶¹ *Hess Warming & Ventilating Co. v. Burlington Grain Elevator Co.*, — Mo. —, 217 S. W. 493.

§ 3459. — Prerequisites and conditions to increase; fees.⁶² An attempted increase of stock is void where statutory requirements are not complied with, including, in Idaho, failure of directors to pass a resolution calling a stockholders' meeting and the failure to give notice of such meeting.⁶³ An increase of stock of a public utility cannot be made in some states without the consent of the public service commission.⁶⁴

§ 3460. — How and by whom increase must be made or authorized. The words "entire capital stock," as used in a statute requiring a favorable vote of at least two-thirds of the entire capital stock to authorize an increase of the capital stock, means the entire issued or subscribed stock and not the entire authorized stock.⁶⁵

§ 3461. Subscription for, and allotment of increase. Ordinarily stockholders cannot be compelled to pay a bonus on subscribing to an increase in stock.⁶⁶

§ 3462. Rights and remedies of existing stockholders as to the increased stock—In general.⁶⁷ Stockholders have a pre-emptive right to subscribe to an increase of the stock.⁶⁸ The relation of stockholder must exist, however, at the time;⁶⁹ and

⁶² Fees, see § 225, supra.

⁶³ Farmers' & Traders' Bank v. National Laundry & Linen Supply Co., 30 Idaho 788, 168 Pac. 670.

⁶⁴ In re Fryeburg Water Co., — N. H. —, 106 Atl. 225.

⁶⁵ Missouri Valley Grocery Co. v. Hall, — N. D. —, 178 N. W. 193.

⁶⁶ Dunn v. Acme Auto & Garage Co., 168 Wis. 128, 169 N. W. 297.

⁶⁷ Pre-emptive right on sale of unissued stock, see § 3479, infra.

Notes on right of stockholder to preference in subscribing for new stock, see Ann. Cas. 1918 B 132, L. R. A. 1918 D 741.

⁶⁸ Kingston v. Home Life Ins. Co., — Del. Ch. —, 101 Atl. 898;

Hammer v. Cash, — Wis. —, 178 N. W. 465.

For note on "right of existing stockholder to subscribe for increase of stock," see L. R. A. 1918 D 741, 742.

Directors who vote a new issue of stock cannot subscribe for it themselves without giving other stockholders a chance to subscribe, especially where there is a long-standing dispute between two factions, both of which are attempting to obtain control. Glenn v. Kittanning Brewing Co., 259 Pa. 510, L. R. A. 1918 D 738 with note, 103 Atl. 340.

⁶⁹ Where stockholders sell a certain number of shares of so-called treasury stock, not yet

an amendment of the charter increasing the capital stock does not obligate the corporation to issue the additional stock nor give a stockholder the right to immediately demand that his proportional share of the entire amount of such increase be issued to him.⁷⁰ However, holders of preferred stock need not be given the right to subscribe to new preferred, where the old preferred has no right in the assets except to the extent of par and accrued dividends, and the relative interest of the old preferred stock will not be affected by the issuance of the new stock.⁷¹

There is no vested right in stockholders to subscribe for an issue of new stock, since the issue of new stock may be on such terms as is voted by the stockholders within the scope of legislative sanction.⁷²

Stockholders may waive their pre-emptive right of subscription to new stock.⁷³

§ 3463. — Transfer or devolution of "rights" to allotment. The right to subscribe to a new issue of stock is capital and not income.⁷⁴ Where a stock dividend was income so as to go to the life estate, the appurtenant subscription right also inures to him.⁷⁵

§ 3464. — Remedies to enforce stockholder's "rights" to allotment or to preserve status. Injunction lies to prevent a corporation committing acts which will make it impossible for a stockholder to exercise his right to purchase his pro rata share of unissued capital stock which is to be issued and sold.⁷⁶

§ 3465. Sale of increase by corporation.⁷⁷

issued or paid for, but which the sellers had agreed between themselves to take, the buyer acquires no right to subscribe for an increase of stock made before his agreement of purchase is carried out. *Levy v. Sattler*, 169 Wis. 308, 172 N. W. 738.

⁷⁰ *Hammer v. Cash*, — Wis. —, 178 N. W. 465.

⁷¹ *General Ins. Co. v. Bethlehem Steel Corporation*, 88 N. J. Eq. 237, 102 Atl. 252.

⁷² *Brown v. Boston & M. R. R.*, 233 Mass. 502, 124 N. E. 322.

⁷³ *General Inv. Co. v. Bethlehem Steel Corporation*, 88 N. J. Eq. 237, 102 Atl. 252.

⁷⁴ *In re Butler's Estate*, 106 N. Y. Misc. 375, 174 N. Y. Supp. 880.

⁷⁵ *In re Baldwin*, 189 N. Y. App. Div. 126, 178 N. Y. Supp. 108.

⁷⁶ *Titus v. Paul State Bank*, 32 Idaho 23, 179 Pac. 514.

⁷⁷ Sale of unissued stock, see § 3479, *infra*.

§ 3467. Overissues and unauthorized increase—In general. An overissue of stock is void and certificates thereof are wholly invalid.⁷⁸ A fortiori, an overissue of stock, after the whole authorized capital stock has been issued, without complying with any of the statutory requirements as to increase of stock, is wholly unauthorized and void.⁷⁹ No one "holding a share of stock void for overissue can compel the real owner so to manipulate the stock books as to deprive him of his share, and by so much the more he cannot by mandamus compel the cashier of a corporation to recognize as valid a certificate void for overissue."⁸⁰ But where a corporation has illegally issued stock in excess of its authorized maximum capital, it has power to contract for a surrender and cancellation of part of the stock to correct the overissue.⁸¹ Stock subscribed, paid for and issued before an excess issue of stock is not affected by the overissue; and if the holder in good faith surrenders his stock to extinguish the overissue, and the rights of others are not affected thereby, the overissue is no defense to an action for the value or the agreed price of the stock surrendered.⁸²

In case of an overissue, a purchaser from the corporation may recover the amount paid as money had and received.⁸³ A bona fide purchaser of overissued stock, who sustains damages, may recover his damages against the officers of the corporation who issued such stock or allowed it to be issued.⁸⁴

§ 3470. Reduction of capital stock.⁸⁵

§ 3471. Authority and procedure to effect reduction; consent of stockholders. A corporation, in reducing its capital, may require a stockholder to accept a certificate for a fractional share

⁷⁸ *Standard Lithographing & Printing Co. v. Twin City Motor Speedway Co.*, 139 Minn. 120, 167 N. W. 796.

⁷⁹ *Leffingwell v. Evans*, 185 Ky. 351, 216 S. W. 58.

⁸⁰ *Mitchell v. Beachy*, 104 Kan. 445, 179 Pac. 365.

⁸¹ *Kelly v. Central Union Fire Ins. Co.*, 101 Kan. 91, L. R. A. 1918 C 1170, 165 Pac. 806.

⁸² *Kelly v. Central Union Fire Ins. Co.*, 101 Kan. 91, L. R. A. 1918 C 1170, 165 Pac. 806.

⁸³ *Citizens' Loan & Savings Co. v. Arwood*, — Ala. App. —, 81 So. 854.

⁸⁴ *Leffingwell v. Evans*, 185 Ky. 351, 216 S. W. 58.

⁸⁵ By purchase of own stock, see § 1135 et seq., supra.

of stock.⁸⁶ The Delaware statute fixing the procedure for amending a charter by increasing or decreasing "authorized" capital stock does not apply where it is sought merely to reduce the amount of stock issued and outstanding.⁸⁷ In Delaware, under the statutes, a corporation cannot, by a vote of two-thirds of all the stockholders, both common and preferred, reduce the stock of each preferred stockholder by two-fifths, with the corporation still a going concern and able to earn profits, as against the objection of dissenting preferred stockholders.⁸⁸

§ 3472. Effect of reduction; rights of creditors.⁸⁹ A reduction of stock does not release liability of officers for squandering assets.⁹⁰ Ordinarily creditors cannot object to a reduction of capital of a corporation where no diminution of unpaid capital or repayment to shareholders of paid-up capital is involved.⁹¹ Where the capital stock has been decreased, it is error, in a suit to compel the corporation to issue a certificate to a stockholder, to order issue of the number of shares he was entitled to before the decrease, especially where in excess of its capital as decreased.⁹²

VII. ISSUE OF STOCK

§ 3476. In whom authority is vested. The propriety of acts of directors in selling unissued stock, several years after the creation of the corporation, to raise money to pay off a debt which could easily be paid out of earnings, is purely a matter of corporate policy with which the courts will not interfere.⁹³ The issuance and sale of stock by the president and secretary to themselves is void where they had no authority to issue it.⁹⁴

⁸⁶ *Perry v. Bank of Commerce*, 118 Miss. 852, 80 So. 332.

⁸⁷ *Kennedy v. Carolina Public Service Co.*, 262 Fed. 803.

⁸⁸ *Kennedy v. Carolina Public Service Co.*, 262 Fed. 803.

⁸⁹ This section of *Fletcher* is cited in *Rice v. Thomas*, 184 Ky. 168, 211 S. W. 428.

⁹⁰ *Perry v. Bank of Commerce*, 118 Miss. 852, 80 So. 332.

⁹¹ *In re Meux's Brewery Co., Ltd.*, [1919] 1 Ch. Div. 28.

⁹² *Selwyn-Brown v. Superno Co.*, 181 N. Y. App. Div. 420, 168 N. Y. Supp. 918.

⁹³ *Thurmond v. Paragon Colliery Co.*, 82 W. Va. 49, 95 S. E. 816, and see § 4065, *infra*.

⁹⁴ *Hammer v. Cash*, — Wis. —, 178 N. W. 465.

§ 3477. Consent of public service commission; Blue Sky Laws. The public service commission has no power to authorize the issuance of stock to reimburse the treasury of a corporation for expenditures already made on capital account, except in so far as the statute itself may authorize it.⁹⁵ A certificate to be issued by a corporation to be organized in the future is a "speculative security," the sale of which is governed by the Blue Sky Law.⁹⁶

§ 3478. When stock is deemed issued.⁹⁷ Stock may be deemed issued before delivery.⁹⁸ Whether stock has been "issued," where paid for by a note, is often, if not usually, a question of fact.⁹⁹

§ 3479. Right of stockholders to preference on issue of stock. The rule in Idaho is that if a part of the authorized capital stock remains unissued, each stockholder, in the absence of a statute to the contrary, has a right to purchase such proportion of it, when the issuance and sale thereof is directed, as his holdings bear to the stock then outstanding.¹ In West Virginia, the pre-emptive right extends to stock issued long after the creation of the corporation and commencement of business.² In Wisconsin, where a corporation purchases its own capital stock and afterwards proposes to reissue it, the rule giving stockholders opportunity to take a proportionate share of increases of stock applies to such reissued stock.³

⁹⁵ *Venner v. Michigan Railroad Commission*, 205 Mich. 573, 172 N. W. 567.

⁹⁶ *State ex rel. Rossen v. Welch*, — N. D. —, 172 N. W. 234.

⁹⁷ Agreement to issue stock as making person a stockholder, see *Doty v. California Rice Milling Co.*, 37 Cal. App. 449, 174 Pac. 389.

Issuance of stock in escrow as payment for land, so as to preclude vendor's lien, see *Doty v. California Rice Milling Co.*, 37 Cal. App. 449, 174 Pac. 389.

⁹⁸ *Lask v. Bedell* (N. J. Ch.), 109 Atl. 849.

What constitutes delivery of stock, see *Tucker v. Scott*, — Cal. —, 186 Pac. 150.

⁹⁹ *Wilson v. Bankers' Trust Co.*, — Tex. Civ. App. —, 218 S. W. 803, and see §§ 3512-3514, *infra*.

¹ *Titus v. Paul State Bank*, 32 Idaho 23, 179 Pac. 514, citing *Fletcher Cyc. Corp.* § 3479.

² See *Thurmond v. Paragon Colliery Co.*, 82 W. Va. 49, 95 S. E. 816.

³ *Dunn v. Acme Auto & Garage Co.*, 168 Wis. 128, 169 N. W. 297.

Offering reissued stock for sale to the highest bidder does not protect a stockholder in his right to acquire his proportionate share of the proposed reissue, especially where the fair value of the stock can only be guessed at.⁴

In authorizing a sale of unissued stock, to increase the working capital, the stockholders may fix the price at which the stock should be sold, and no stockholder can complain thereof where all shareholders are given the right to purchase their pro rata shares at the price fixed.⁵

VIII. ISSUE AND CANCELLATION OF CERTIFICATES OF STOCK

§ 3482. Form and contents of certificate. A certificate of stock is not invalid because not signed by the registrar.⁶

§ 3483. Right to certificate. An incorporator stated to be the owner of a certain number of shares, in the articles of incorporation, is a stockholder, so far as the corporation is concerned, and entitled to a certificate of stock, regardless of any arrangements with third persons as to payment for the stock.⁷

§ 3484. Remedies for refusal to issue certificates.⁸ A suit in equity, as distinguished from an action at law, lies to compel a transfer of stock on the books, or to issue to plaintiff a certificate of stock where it has wrongfully cancelled his certificate.⁹ In Missouri, however, it is held that an action at law against the corporation is the proper remedy where it refuses to issue a certificate of stock to the owner.¹⁰ Refusal by a corporation to issue stock to one entitled thereto may or may not constitute conversion according to the character of the excuse for not issuing the stock.¹¹ Mandamus lies to compel the issuance of certificates of stock, in some jurisdictions.¹²

⁴ *Dunn v. Acme Auto & Garage Co.*, 168 Wis. 128, 169 N. W. 297.

⁵ *Thurmond v. Paragon Colliery Co.*, 82 W. Va. 49, 95 S. E. 816.

⁶ *Hudson Trust Co. v. American Linseed Co.*, 190 N. Y. App. Div. 289, 180 N. Y. Supp. 17.

⁷ *Williams v. Everett*, — Mo. —, 200 S. W. 1045.

⁸ See also § 3817 et seq., *infra*.

⁹ *Selwyn-Brown v. Superno Co.*, 181 N. Y. App. Div. 420, 168 N. Y. Supp. 918.

¹⁰ *Williams v. Everett*, — Mo. —, 200 S. W. 1045.

¹¹ *Baglin v. Earl-Eagle Min. Co.*, — Utah —, 184 Pac. 190.

¹² *Capitci Petroleum Co. v. Haldeman*, — Colo. —, 180 Pac. 758, holding that there was no

A broker to whom stock is assigned for sale, although based on no consideration, is the real party in interest so as to be entitled to sue the corporation for refusal to issue certificates.¹³

§ 3485. Cancellation of certificates. A court of equity has power to cancel stock issued wrongfully or without authority, at the suit of the corporation,¹⁴ at least where holders are to be saved harmless,¹⁵ or to cancel stock certificates which should have been returned to the corporation.¹⁶

A corporation cannot sue to cancel shares of stock on account of failure to pay subscriptions where the stock is in the hands of bona fide purchasers for value.¹⁷ Where there are no creditors, and the issuance of stock for property is approved by all the stockholders, the corporation cannot sue to cancel such stock.¹⁸ Stock issued to a director or officer for services in reorganizing the company, as valued by the board of directors, will not be cancelled, in the absence of fraud, although the compensation may have been excessive.¹⁹ A corporation cannot obtain a cancellation of stock issued to an employee for services to be rendered, on the ground that he misrepresented his qualifications, where he had been permitted to perform services for five years and there is nothing to show that he did not perform the services called for by his contract.²⁰

A cause of action in favor of a corporation to cancel stock issued by it commences to run, where there is no fraud, when the stock is alleged to have been unlawfully issued.²¹

“plain, speedy and adequate remedy” by an action for damages or a suit in equity; and see § 3818, *infra*.

¹³ *Baglin v. Earl-Eagle Min. Co.*, — Utah —, 184 Pac. 190.

¹⁴ *Rice v. Thomas*, 184 Ky. 168, 211 S. W. 428, quoting *Fletcher Cyc. Corp.* § 3485.

Validity of stock issued can be determined only by a suit in equity. *Hammer v. Cash*, — Wis. —, 178 N. W. 465.

¹⁵ *Copper King Min. Co. v. Hanson*, — Utah —, 176 Pac. 623.

¹⁶ *American Forging & Socket*

Co. v. Wiley, 206 Mich. 664, 173 N. W. 515.

¹⁷ *Damron v. Denny*, 149 Ga. 280, 99 S. E. 851.

¹⁸ *East Lake Lumber Co. v. Van Gorder*, 105 N. Y. Misc. 704, 174 N. Y. Supp. 38.

¹⁹ *Colonial Biscuit Co. v. Oreutt*, 264 Pa. 40, 107 Atl. 315.

²⁰ *Devonian Products Co. v. Webster*, — Iowa —, 177 N. W. 513.

²¹ An action by a corporation to cancel stock issued by an officer to himself is barred in New York, in ten years from the time the

Except as against creditors, a surrender of stock by the stockholders, its cancellation, and a reissue and redistribution of the stock, is valid; and a creditor receiving stock in payment of his claim is no longer a creditor.²²

IX. UNAUTHORIZED AND FICTITIOUS STOCK AND CERTIFICATES

§ 3487. Certificate as a representation of validity, ownership and power to convey.²³

§ 3488. Estoppel to deny validity.²⁴ Stockholders are estopped to deny personal liability to creditors on unpaid stock, on the ground that the stock held by them was wrongfully issued.²⁵ A person holding himself out as the owner of preferred stock is estopped to deny his liability as stockholder to creditors for unpaid subscriptions, on the ground that his stock was illegally issued and void.²⁶

§ 3489. Stolen certificates.²⁷

§ 3490. Forged certificates.²⁸

§ 3491. Authority of officer or agent issuing certificate. A corporation is estopped to dispute the authority of its officers to issue a certificate of stock, within the apparent scope of their authority, after it has come into the hands of an innocent purchaser for value.²⁹

§ 3492. Certificates signed in blank. Where the president and the treasurer, the two officers authorized to sign certificates

stock was unlawfully issued. *East Lake Lumber Co. v. Van Gorder*, 105 N. Y. Misc. 704, 174 N. Y. Supp. 38.

²² *Standard Lithographing Co. v. Twin City Motor Speedway Co.*, 139 Minn. 120, 167 N. W. 347.

²³ Remedy, see § 3493, *infra*.

²⁴ Estoppel to dispute authority of officers to issue, see § 3491, *infra*.

²⁵ *Shugart v. Maytag*, — Iowa —, 176 N. W. 886.

²⁶ *Du Pont v. Ball*, — Del. —, 106 Atl. 39, modifying *John W. Cooney Co. v. Arlington Hotel Co.*, — Del. Ch. —, 101 Atl. 879.

²⁷ See § 3491, *infra*.

²⁸ See §§ 3491, 3492, *infra*.

²⁹ *Green v. Caribou Oil Min. Co.*, 179 Cal. 787, 178 Pac. 950, citing *Smith v. Martin*, 135 Cal. 251, 67 Pac. 779. See also § 3497, *infra*.

of stock, signed quantities of them in blank and delivered them to a clerk, giving him power to fill in and deliver them, and the certificates so signed were left loose in a vault open to employees, and the directors exercised no supervision over the issuance, the loss, in case stock is fraudulently issued by the clerk to an innocent third person, is on the corporation.³⁰

§ 3493. **Liability of corporation in damages.** An action on the common counts will not lie to recover on an implied warranty that stock represented by a certificate was valid.³¹

§ 3493a [New]. **Liability of officers issuing the stock.** Officers of a corporation are personally liable for a fraudulent issue of stock, or stock issued in violation of law.³²

§ 3494. **Remedies of the corporation.** Stock may be cancelled, where unauthorized, in a proper case.³³ Fictitious stock, issued wholly or partially without consideration in violation of the constitution or a statute, will be cancelled in equity on a proper application, and it follows, of course, that stockholders cannot enjoin such a cancellation by the directors.³⁴

§ 3497. **Persons entitled to protection or relief.** The rule that a person dealing with the officers of a corporation concerning corporate property, where the consideration is personal to the officer, must inquire as to his authority, does not apply to a pledgee of stock issued to the secretary of the corporation in his name and which appears to have been his property for several months.³⁵ Where a certificate of stock is fraudulently issued by the secretary and transfer agent to himself, all in due form, the rights of a pledgee of the stock are superior to those of the corporation under the rule that where one of two innocent persons must suffer, etc.³⁶ A statutory provision that a transfer of

³⁰ *Hudson Trust Co. v. American Linseed Co.*, 190 N. Y. App. Div. 289, 180 N. Y. Supp. 17.

³¹ *Randle v. Walker*, — Ala. App. —, 84 So. 551.

³² *Fish v. White*, — Iowa —, 175 N. W. 748.

³³ *Rice v. Thomas*, 184 Ky. 168, 211 S. W. 428, quoting *Fletcher Cyc. Corp.* § 3494.

³⁴ *Rice v. Thomas*, 184 Ky. 168, 211 S. W. 428.

³⁵ *Green v. Caribou Oil Min. Co.*, 179 Cal. 787, 178 Pac. 950, citing *Smith v. Martin*, 135 Cal. 251, 67 Pac. 779.

³⁶ *Green v. Caribou Oil Min. Co.*, 179 Cal. 787, 178 Pac. 950.

shares of stock "is not valid except as to the parties thereto," until entered on the books of the corporation, does not affect the validity of a pledge of stock issued by the secretary and transfer agent to himself without authority and fraudulently.³⁷

X. RIGHTS AND REMEDIES IN CASE OF LOSS OF CERTIFICATE OF STOCK

§ 3498. Right to new certificate.³⁸ If a certificate of stock is lost, the court may order a new one issued on filing a bond in favor of any person thereafter appearing to be the lawful owner of the lost certificate.³⁹

XI. PAYMENT FOR STOCK

§ 3503. Payment in property, labor or services—The right in general. All of the stock may be issued for property where any part may be so issued, in the absence of a statute to the contrary.⁴⁰ A vote of the stockholders that no stock other than a specified amount should be issued except for cash is binding on the board of directors so as to prevent it lawfully issuing stock in excess of such amount, for services rendered.⁴¹ A formal resolution is not necessary to warrant the issuance of stock for property, where the issuance was acquiesced in by all the stockholders, and was a part of the plan underlying the formation and organization of the corporation.⁴²

The validity of stock issued for property depends on the law of the state where the corporation was created, where not against the public policy of the state in which suit is brought to cancel such stock.⁴³

³⁷ *Green v. Caribou Oil Min. Co.*, 179 Cal. 787, 178 Pac. 950, criticizing *Whitfield v. Nonpareil Consol. Copper Co.*, 67 Wash. 286, 41 L. R. A. (N. S.) 187, 123 Pac. 1078.

³⁸ Note on "right of stockholder to compel duplication of lost certificate," see *Ann. Cas.* 1918 E 66.

³⁹ *In re Francis*, — Del. —, 108 Atl. 31.

⁴⁰ *Sargent v. Palace Café Co.*, 175 Cal. 737, 167 Pac. 146.

⁴¹ *United German Silver Co. v. Bronson*, 92 Conn. 266, 102 Atl. 647.

⁴² *East Lake Lumber Co. v. Van Gorder*, 105 N. Y. Misc. 704, 174 N. Y. Supp. 38.

⁴³ *Taylor v. Citizen's Oil Co.*, 182 Ky. 350, 206 S. W. 644; *Axford v. Western Syndicate Inv. Co.*, 141 Minn. 412, 170 N. W. 587.

§ 3504. — Charter, statutory or constitutional provisions. A credit is not "cash."⁴⁴ A subscriber for nearly all the stock of a corporation which has become bankrupt cannot, under a statute requiring payment of the subscription in money, discharge his liability by turning in assets of another corporation worth less than half the amount of the subscription, but is liable for assessment for the balance.⁴⁵ Failure of the directors to perform the statutory duty of placing on the record the payments for stock otherwise than by cash, does not raise a presumption that certain stock not so recorded was paid for in cash.⁴⁶

In some states, by statute, subscriptions to stock in property are valid only where authorized by the stockholders at a meeting; and consent of all the directors is not sufficient although all stockholders are directors, since prospective purchasers of stock would look to the records of stockholders' rather than directors' meetings.⁴⁷

The Iowa statute providing that stock issued in violation of the statute forbidding issuance except for cash shall be "void" is to be construed as meaning "voidable."⁴⁸

In Iowa, failure to obtain permission from the Executive Council to sell stock for other than cash does not make the stock void so as to invalidate notes given therefor.⁴⁹

§ 3505. — Payment in services.⁵⁰ Stock may be issued for services, where there is no statute or vote to the contrary.⁵¹ A corporate contract to pay for services with a certain amount of

⁴⁴ *Citizens' Nat. Bank v. Stevenson*, — Tex. Civ. App. —, 211 S. W. 644.

⁴⁵ *In re Louis J. Bergdoll Motor Co.*, 260 Fed. 234.

⁴⁶ *United German Silver Co. v. Bronson*, 92 Conn. 266, 102 Atl. 647.

⁴⁷ *McGaw v. Hoen*, 133 Md. 672, 106 Atl. 13.

⁴⁸ *Ramsay v. Crevlin*, 254 Fed. 813.

⁴⁹ *Sherman v. Smith*, 185 Iowa 654, 169 N. W. 216.

⁵⁰ See also § 3524, *infra*.

⁵¹ *United German Silver Co. v.*

Bronson, 92 Conn. 266, 102 Atl. 647.

Directors have power to order a transfer of stock to an officer of the company as compensation for services in organizing the company and conducting its business. *Batchellor v. Olmsted*, 261 Fed. 533.

If stock is voted to a promoter in payment for his services, a stockholder cannot enjoin delivery of such stock. *Decke v. Baker*, 201 Mich. 608, 167 N. W. 908.

stock is not illegal because it is afterwards discovered that the value of the services was less than the value of the stock of the newly-created corporation.⁵²

Stock cannot be issued as full paid and nonassessable for services to be rendered in the future, where the Constitution forbids issuance of stock except for labor "done," etc.⁵³ But there is a difference, so far as the right to issue stock for services is concerned, between a contract to issue stock in advance of the services to be rendered, and one to issue stock for future services but not until such services were performed.⁵⁴ Thus, an agreement to issue shares of stock "in payment of amounts to become due" for services "to be rendered" to the company "to its satisfaction" does not provide for issuance of stock for services to be rendered in the future so as to violate the New York statutes.⁵⁵

The fact that the capital of a company increases in value, after its organization, by performance of certain voluntary labor by stockholders, does not operate as a payment by said stockholders on their stock so as to defeat an action by creditors on unpaid stock.⁵⁶

Services rendered "before" incorporation are not "cash" or "property" for which stock may be issued, in New York.⁵⁷

Stock issued as a bonus for a loan to the corporation is not issued for "services" so as to be within a statute authorizing issuance of stock for "services" or for property.⁵⁸

Good-will and influence in promoting the construction of a railroad are no consideration for stock of a railroad company.⁵⁹

In an action on a stock subscription the contention that be-

⁵² *Morgan v. Bon Bon Co.*, 222 N. Y. 22, 118 N. E. 205, rev'g 165 N. Y. App. Div. 89, 150 N. Y. Supp. 668.

⁵³ *Scully v. Automobile Finance Co.*, — Del. Ch. —, 109 Atl. 49.

Inasmuch as the statute in New York forbids the issuance of stock except for labor "done," stock cannot be issued for future services as corporate officers. *Palmer v. Scheftel*, 183 N. Y. App. Div. 77, 170 N. Y. Supp. 588.

⁵⁴ *Morgan v. Bon Bon Co.*, 222 N. Y. 22, 118 N. E. 205, rev'g 165

N. Y. App. Div. 89, 150 N. Y. Supp. 668.

⁵⁵ *Morgan v. Bon Bon Co.*, 222 N. Y. 22, 118 N. E. 205, rev'g 165 N. Y. App. Div. 89, 150 N. Y. Supp. 668.

⁵⁶ *In re Caledonia Coal Co.*, 254 Fed. 742, 746.

⁵⁷ *American Macaroni Corporation v. Saumer*, — N. Y. Misc. —, 174 N. Y. Supp. 183.

⁵⁸ *Hopper v. Brodie*, 134 Md. 290, 106 Atl. 700.

⁵⁹ *Razor v. West Coast Development Co.*, — Ore. —, 192 Pac. 631.

cause the corporation has received the benefit of the services rendered as a consideration for the stock it is estopped to deny that the services constituted payment of defendant's stock subscriptions, cannot be sustained where to do so would protect the directors on contracts authorized by themselves under circumstances that establish not only illegality but such a breach of fiduciary relations as amounts to bad faith.⁶⁰

The maker of a note given on a subscription to stock is liable for the amount in cash, where sued by a receiver after the corporation is insolvent, though the note was delivered under an agreement that it was to be paid in labor.⁶¹

§ 3506. — General nature of property that may be taken. Assignment to a corporation of a plan of business, where without novelty and having no element of property, is not "property" acquired by the corporation for which stock may be issued.⁶² Contracts of agency with automobile manufacturers are not such property that stock can be issued therefor, since mere contemplated profits, at least under the Delaware law.⁶³ A subscription payable in land is valid where the corporation has power to acquire the land.⁶⁴

§ 3507. Patents, trade-marks, secret formulæ, etc. A process, although without assignable or market value, may be a good consideration for the issue of stock.⁶⁵

§ 3511. — Further illustrations. Good-will of a corporation may have a money value which may be used in payment of stock of another company to the extent of its value; ⁶⁶ but good-will of

⁶⁰ *Palmer v. Scheftel*, 183 N. Y. App. Div. 77, 170 N. Y. Supp. 588.

⁶¹ *Baber v. De Camp*, 96 S. C. 432, 6 A. L. R. 275, 81 S. E. 155, distinguishing *Nettles v. Marco*, 33 S. C. 47, 11 S. E. 595.

Note on "liability upon stock subscription payable in services which are rendered unnecessary by the insolvency of the corporation, or other cause," see 6 A. L. R. 277, annotating *Baber v. De Camp*, 96 S. C. 432, 6 A. L. R. 275, 81 S. E. 155.

⁶² *Scully v. Automobile Finance Co.*, — Del. Ch. —, 109 Atl. 49.

⁶³ *Wallace v. Weinstein*, 257 Fed. 625, 631.

⁶⁴ *Natwick v. Terwilliger*, 24 Wyo. 253, 160 Pac. 338.

⁶⁵ *Kunkle v. Soule*, — Colo. —, 190 Pac. 536.

⁶⁶ *Foote v. Bowman*, 210 Ill. App. 631. See also *William E. Dee Co. v. Proviso Coal Co.*, 212 Ill. App. 400.

a failing business is merely an imaginary quantity and has no money value which can be turned in for stock.⁶⁷

If it is agreed that one becoming connected with a corporation may purchase shares to be paid for out of dividends, he cannot obtain the stock by any other mode of payment.⁶⁸

§ 3513. Payment in notes, bonds, mortgages, etc.—Effect of charter or statutory provisions. Where stock can be paid for only in money, a note is not payment.⁶⁹ A promissory note given for stock is not “property actually received,” within the Texas Constitution.⁷⁰ A note is not “property” for which stock may be issued, under the Texas Constitution, although collateral security was deposited,⁷¹ but a later case in Texas holds that a subscriber’s note secured by a valid first mortgage on real estate is “property” for which stock may be issued.⁷² Where a note is given for stock in violation of the Texas constitutional provision, the stock is not void.⁷³

Giving notes for stock does not violate constitutional or statutory provisions prohibiting “issuance” of stock except for money paid, etc., where the stock was not to be delivered until the notes were paid, since there is no “issuance” without delivery.⁷⁴

⁶⁷ *Hodde v. Hahn*, — Mo. —, 222 S. W. 799.

⁶⁸ *McCormick v. Badham*, — Ala. —, 85 So. 401.

⁶⁹ *Wing v. McCallum*, 244 Fed. 199, 206; *Thompson v. First State Bank*, — Tex. Civ. App. —, 189 S. W. 116.

⁷⁰ *Thompson v. First State Bank*, 109 Tex. 419, 211 S. W. 977, aff’g — Tex. Civ. App. —, 189 S. W. 116; *Washer v. Smyer*, 109 Tex. 398, 211 S. W. 985; *Rousseau v. Everett*, — Tex. Civ. App. —, 209 S. W. 460; *Mitchell v. Porter*, — Tex. Civ. App. —, 194 S. W. 981.

⁷¹ *Shield v. Lone Star Life Ins. Co.*, — Tex. Civ. App. —, 202 S. W. 211.

⁷² *Prudential Life Ins. Co. v. Pearson*, — Tex. —, 222 S. W.

967, rev’g — Tex. Civ. App. —, 188 S. W. 513; *General Bonding & Casualty Ins. Co. v. Moseley*, — Tex. —, 222 S. W. 961, rev’g — Tex. Civ. App. —, 174 S. W. 1031.

⁷³ *Thompson v. First State Bank*, 109 Tex. 419, 211 S. W. 977.

⁷⁴ *Smith v. McAdams*, — Tex. Civ. App. —, 206 S. W. 955; *Zapp v. Spreckels*, — Tex. Civ. App. —, 204 S. W. 786; *McCoy v. Bankers’ Trust Co.*, — Tex. Civ. App. —, 200 S. W. 1138.

If the stock is not to be issued until the note given therefor is paid, there can be no complaint that the stock was not “issued” for money. *Zapp v. Spreckels*, — Tex. Civ. App. —, 204 S. W. 786.

But the fact that there was no manual delivery of stock and

But it is now held in Texas, reversing earlier decisions, that stock cannot be issued for notes, although the stock is not delivered, where the subscriber is paid the dividends and otherwise recognized as a stockholder.⁷⁵

Stock may be sold for securities where, by statute, property may be received for stock; "securities" not meaning notes of the subscriber.⁷⁶

The fact that a statute forbids issuance of stock for promissory notes does not invalidate an agreement by a purchaser of stock who had given a note therefor to reimburse directors if they would pay for the stock already issued.⁷⁷

§ 3514. — Enforceability of notes. In the federal courts, a note given for stock is enforceable in the hands of a bona fide holder.⁷⁸ Federal courts are not bound to follow the state courts as to questions of general commercial law, such as the validity of a note given for stock where the state constitution forbids issuance of stock except for money, etc.⁷⁹

In Texas the rule formerly was that the note was unenforceable,⁸⁰ but it is now held that such a note is enforceable in the

that the certificate was not made out for a year does not necessarily show that there was not a sale of stock in exchange for notes, in violation of the constitution. *Cattlemen's Trust Co. v. Swearingen*, — Tex. Civ. App. —, 200 S. W. 596.

⁷⁵ *Pruett v. Cattlemen's Trust Co.*, — Tex. —, 222 S. W. 533, rev'g — Tex. Civ. App. —, 184 S. W. 716.

A constitutional prohibition against issuing stock except for money paid, etc., applies not only where a certificate is issued but also "to prohibit the exercise by the subscriber of the rights of a stockholder and the recognition on the part of the corporation of such right" where no certificate is issued on the giving of a note. *Turner v. Cattlemen's Trust Co.*, — Tex. —, 215 S. W. 831.

⁷⁶ *Commonwealth Bonding & Casualty Ins. Co. v. Hollifield*, — Tex. —, 220 S. W. 322.

⁷⁷ *Ramsay v. Crevlin*, 254 Fed. 813.

⁷⁸ *Wilson v. Spencer*, 261 Fed. 357.

⁷⁹ *Wilson v. Spencer*, 261 Fed. 357.

⁸⁰ *Lone Star Life Ins. Co. v. Pierce*, — Tex. Civ. App. —, 200 S. W. 1104.

The rule that a subscription note is unenforceable where a constitutional provision prohibits the issuance of stock except for money, labor or property, applied where the question was whether the stock for which the note was given had in fact been issued. *Turner v. Cattlemen's Trust Co.*, — Tex. —, 215 S. W. 831.

Since in Texas a note given for a subscription to stock is illegal,

hands of a bona fide purchaser for value,⁸¹ although not in the hands of a transferee with notice of the consideration.⁸² It is also held in Texas that a stockholder sued by representatives of the corporation after insolvency on a note given for stock is estopped to set up the invalidity of his subscription because not paid for in cash.⁸³ As against creditors of the corporation, a subscriber to stock who gave his note therefor is estopped to set up its invalidity on the theory that stock can be issued only for property, etc.⁸⁴

In Iowa, a note given for corporate stock, in violation of the Iowa statute requiring permission from the Executive Council where stock is issued for something other than cash, is not void, although the statute makes stock issued in violation thereof "void," since the word "void" will be construed as "voidable" because of other provisions in the statutes.⁸⁵

A subscriber may sue to cancel notes and a deed of trust given for his subscription, where the note and deed are void because of the want of power of the corporation to issue stock except for money.⁸⁶ A subscriber to stock who gave his note therefor cannot defend an action on the note on the ground of want of consideration where he had transferred the stock for a valuable consideration, notwithstanding a statute forbids issuance of stock except for cash.⁸⁷

the corporation cannot collect it. *Shield v. Lone Star Life Ins. Co.*, — Tex. Civ. App. —, 202 S. W. 211.

⁸¹ *Wilson v. Spencer*, 261 Fed. 357; *Thompson v. First State Bank*, 109 Tex. 419, 211 S. W. 977, aff'g — Tex. Civ. App. —, 189 S. W. 116; *Washer v. Smyer*, 109 Tex. 398, 211 S. W. 985, overruling *Republic Trust Co. v. Taylor*, — Tex. Civ. App. —, 184 S. W. 773.

A note given for stock, although in violation of the constitution, is not void but is valid in the hands of a holder in due course, where the constitution does not provide that stock so issued shall be "void." *Washer v. Smyer*, 109 Tex. 398, 211 S. W. 985.

⁸² *Citizens' Nat. Bank v. Stevenson*, — Tex. Civ. App. —, 211 S. W. 644.

⁸³ *Thompson v. First State Bank*, 109 Tex. 419, 211 S. W. 977, aff'g — Tex. Civ. App. —, 189 S. W. 116.

⁸⁴ *Mitchell v. Porter*, — Tex. —, 223 S. W. 197.

⁸⁵ *Sherman v. Smith*, 185 Iowa 654, 169 N. W. 216; *First Nat. Bank v. Fulton*, 156 Iowa 734, 137 N. W. 1019.

⁸⁶ *Mitchell v. Porter*, — Tex. Civ. App. —, 194 S. W. 981.

⁸⁷ *Ramsay v. Crevlin*, 254 Fed. 813.

A subscriber who gave his note for stock, and then indorsed the certificate to one who paid the corporation for the stock, is not liable on the note.⁸⁸

§ 3515. Issue of stock in payment of debts. Where the stockholders consent, stock may be issued to one who had conducted the business for years, to represent profits undrawn by him but credited to him on the corporate books.⁸⁹

XII. WATERED OR FICTITIOUSLY PAID UP STOCK

§ 3519. Powers of corporation at common law—Issue of stock for property, labor or services.⁹⁰ Stock cannot be said to be full paid, so as not to be subject to assessment in bankruptcy proceedings, where it was issued in consideration of a transfer of property which was never made, although the stock was described as full paid.⁹¹

§ 3520. — Issue of stock gratuitously, or at a discount, or as a bonus. Whether the corporation is solvent or insolvent, holders of bonus stock are liable for its par value where the interests of the corporation so demand or it is necessary to hold them liable to pay creditors or if for any reason it is equitable and just to hold them liable.⁹² Where incorporators, after the creation of the corporation, convey certain mining properties owned by them to the corporation in consideration of its whole capital stock, and then returned to the corporation three-fourths of the stock as treasury stock for use in financing the undertaking, whereupon the corporation issued bonds which it sold to the incorporators and others, giving as a bonus one share of treasury stock for each dollar of bonds subscribed, the transaction is valid where the stock is full paid.⁹³ Holders of common stock illegally issued as a bonus to holders of preferred

⁸⁸ Perkins v. Le Viness, 134 Md. 252, 106 Atl. 705.

⁸⁹ Beaman v. Gerrish, — Mass. —, 126 N. E. 352.

⁹⁰ See also §§ 3505, 3506, 3511, supra.

⁹¹ Wallace v. Weinstein, 257 Fed. 625.

⁹² Scully v. Automobile Finance Co., — Del. Ch. —, 109 Atl. 49, noting that New York cases are to the contrary and distinguishing decisions in states where the stock is declared by statute to be void.

⁹³ Clinton Mining & Mineral Co. v. Jamison, 256 Fed. 577, 581.

stock have no right of recovery, as between themselves, on the theory that they are not all in *pari delicto*, merely because some of the preferred stockholders were given a larger proportion of common stock than others.⁹⁴

It seems that the making of a loan to a corporation in bad financial condition may be a valuable consideration for the issuance of stock as a bonus.⁹⁵

§ 3521a [New]. — Issue of balance of stock. Stockholders have the right to fix the price at which the balance of unissued stock shall be sold, to increase the working capital some years after the creation of the corporation; and the fixing of the price at which the balance of unissued stock should be sold, by the directors and stockholders, should not be changed by a court, where not fraudulent, since a matter relating to internal management.⁹⁶ A corporation, the value of whose capital stock has become impaired, may sell additional stock at the real worth or market value thereof, in which case the purchaser does not incur any liability as in case of unpaid stock where he buys below par.⁹⁷

§ 3524. — Payment of commissions and expenses out of proceeds. Statutory prohibition against issuance of stock for any sum less than par value does not, in Wisconsin, prohibit payment of expenses incident to and necessarily incurred in the sale of the stock, including commission contracts.⁹⁸

§ 3525. Charter provisions and statutes and constitutional regulations—In general. By statute in some states, corporations cannot issue stock at less than par.⁹⁹ A constitutional prohibition against "all fictitious increase of stock" precludes an increase of stock of the par value of one dollar, so far as sold for seven cents.¹

⁹⁴ *Hoffard v. Williams Shoe Co.*,
95 Ohio St. 376, 117 N. E. 17.

⁹⁵ *J. F. Lucey Co. v. McMullen*,
— Cal. —, 173 Pac. 1000.

⁹⁶ *Thurmond v. Paragon Colliery Co.*, 82 W. Va. 49, 95 S. E. 816, and see § 4065, *infra*.

⁹⁷ *Thoms & Brennehan v. Goodman*, 254 Fed. 39.

⁹⁸ *Denis v. Nu-Way Puncture Cure Co.*, 170 Wis. 333, 175 N. W. 95.

⁹⁹ *Tramp v. Murquesen*, — Iowa —, 176 N. W. 977.

¹ *Fox v. Seattle Contact Copper Co.*, 98 Wash. 557, 168 Pac. 185.

Where stock cannot be issued for property except at its true market value, stock of a consolidated company cannot be issued to a constituent company share for share but only to the extent that the value of its assets equals the face of the stock issued.² On consolidation of two corporations, stock of the consolidated company issued for stock of a constituent company is not invalid because in the state where the constituent company was created stock could be and was freely exchanged for property without regard to value, while in the state where the consolidation was had stock could not be issued for property except for value received.³

Bonus stock given as an inducement to buy preferred stock is "void" where the constitution forbids the issuance of stock except for money, labor done or property actually received.⁴

§ 3528. — Arizona. One who turns in worthless mining leases for stock is not a "bona fide subscriber" within a constitutional provision that no corporation shall issue stock except to bona fide subscribers.⁵

§ 3532. — Connecticut. A vote by stockholders that no stock be issued except for cash cannot be evaded by the directors by issuing stock in payment for services; but where the corporation afterwards sued the holders of such stock for its par value the irregularity in its issuance was waived.⁶

§ 3538. — Illinois. In Illinois, if any proportion of the capital is paid in property the claim must be appraised by the commissioners and the fair cash value thereof reported.⁷ Failure to observe the requirements of the statute requiring that property transferred for stock shall be appraised and its fair cash value reported by the commissioners does not ipso facto create a liability for a stock subscription.⁸

² Taylor v. Citizens' Oil Co., 182 Ky. 350, 206 S. W. 644.

³ Taylor v. Citizens' Oil Co., 182 Ky. 350, 206 S. W. 644.

⁴ Lavell v. Bullock, — N. D. —, 174 N. W. 764.

⁵ Frame v. Mahoney, — Ariz. —, 187 Pac. 584.

⁶ United German Silver Co. v.

Bronson, 92 Conn. 266, 102 Atl. 647.

⁷ Sherman v. Hayes, 203 Ill. App. 198, holding parties cannot fix fair cash value; Central Trust Co. v. Crawford, 201 Ill. App. 555.

⁸ Central Trust Co. v. Crawford, 201 Ill. App. 555.

§ 3540. — **Iowa.** In Iowa, a statute requires permission from the Executive Council where it is proposed to issue stock for something other than cash.⁹

§ 3542. — **Kentucky.** In Kentucky, stock cannot be issued for labor or services unless the market value thereof is equal to the par value of the stock.¹⁰

§ 3544. — **Maine.**¹¹

§ 3545. — **Maryland.** In Maryland the issuance of stock for property is to be determined by the stockholders and not by the directors, and it is not sufficient that consent be shown by the record of a directors' meeting even where all of the stockholders are directors.¹²

§ 3555. — **New Jersey.** The New Jersey statute requiring the filing of a true statement of the transaction where stock is issued for property does not require the filing of such statement at the time the stock is issued but it may be filed later; and even if it is filed too late such stock is not invalidated so as to excuse a subsequent buyer from performing his contract.¹³

§ 3565. — **South Dakota.** In South Dakota, all fictitious increase of stock is declared void.¹⁴

§ 3567. — **Texas.**¹⁵

§ 3571. — **Washington.** In Washington a stock subscription may be made in property.¹⁶

§ 3572. — **West Virginia.**¹⁷

⁹ *Sherman v. Smith*, 185 Iowa 654, 169 N. W. 216, and see § 3504, supra.

¹⁰ *Detroit-Kentucky Coal Co. v. Bickett Coal & Coke Co.*, 251 Fed. 542; *Taylor v. Citizens' Oil Co.*, 182 Ky. 350, 206 S. W. 644. See also *Jones v. Bowman*, 181 Ky. 722, 205 S. W. 923.

¹¹ See § 3576, infra.

¹² *McGaw v. Hoen*, 133 Md. 672,

106 Atl. 13, and see § 3504, supra, and § 3576, infra.

¹³ *Bartley v. Lindabury*, 89 N. J. Eq. 8, 104 Atl. 333.

¹⁴ *Axford v. Western Syndicate Inv. Co.*, 141 Minn. 412, 170 N. W. 587.

¹⁵ See §§ 3513, 3514, supra.

¹⁶ *Fogarty v. Hunter*, 83 Ore. 183, 162 Pac. 964.

¹⁷ See § 3576, infra.

§ 3573. — **Wisconsin.** The statutory provision that stock shall not be sold at less than par does not prevent payment to an agent selling the stock of twenty-five per cent commission for sale of the stock.¹⁸

§ 3576. **Valuation of property, labor or services received—In general.**¹⁹ The value of property turned in for stock has been said to be “what a reasonably prudent investor who contemplated spending his own money would have been willing to pay for the * * * claims under the circumstances under which the corporators acted on the date of the transfer.”²⁰ In valuing property turned in for stock, the stockholder, when sued by creditors of the corporation, is to be credited with the amount for which the “property would have sold on the day it was transferred to the corporation, assuming a seller willing but not compelled to buy, and a buyer willing but not compelled to buy.”²¹ A margin will be allowed for honest differences of opinion as to value.²² Even under the “true value” rule, the courts give stockholders the benefit of a doubt where there is ground for difference of opinion as to the value of the property.²³ The question of value must be determined upon facts as they existed when the transaction was consummated, and not by subsequent events.²⁴ The issuance of stock at less than par, where forbidden by statute, is fraudulent, without regard to the intent.²⁵ Under a statute making the valuation of directors conclusive, they have no power to adjudge the value of future services.²⁶ A conscious overvaluation by directors is actual fraud and makes the subscription contract unlawful.²⁷

¹⁸ *Denis v. Nu-Way Puncture Cure Co.*, — Wis. —, 175 N. W. 95.

¹⁹ The “true value” rule as opposed to the “good faith” rule, see *Clinton Mining & Mineral Co. v. Jamison*, 256 Fed. 577, citing *Fletcher Cyc. Corp.* § 3576.

²⁰ *Hasson v. Koeberle*, — Cal. —, 181 Pac. 387.

²¹ *William E. Dee Co. v. Proviso Coal Co.*, 212 Ill. App. 400, 408.

²² *Goodman v. White*, 174 N. C. 399, 93 S. E. 906.

Stock may be issued for property, and the valuation put on

the property in good faith cannot be attacked. *Caldwell v. Robinson*, 179 N. C. 518, 103 S. E. 75.

²³ *Clinton Mining & Mineral Co. v. Jamison*, 256 Fed. 577, 582.

²⁴ *Clinton Mining & Mineral Co. v. Jamison*, 256 Fed. 577, 583, citing *Fletcher Cyc. Corp.* § 3576.

²⁵ *Whitewater Tile & Pressed Brick Mfg. Co. v. Johnson*, — Wis. —, 175 N. W. 786.

²⁶ *Scully v. Automobile Finance Co.*, — Del. Ch. —, 109 Atl. 49.

²⁷ *Scully v. Automobile Finance Co.*, — Del. Ch. —, 109 Atl. 49.

In California, stockholders are liable as on unpaid subscriptions where they turn in property for stock at a grossly excessive figure, notwithstanding the honest belief of the directors as to the value of the property at the time of the exchange.²⁸ In Delaware, conscious gross overvaluation of the value of labor, by the directors, is "actual fraud," within the statute excepting from conclusiveness of directors' valuation cases of actual fraud.²⁹ In Maine, by statute, where stock is exchanged for property, the judgment of the directors as to the value of the property is conclusive, in the absence of actual fraud; and creditors who seek to hold such a stockholder liable as for a partly unpaid subscription must allege and show facts showing actual fraud.³⁰ In Maryland, by statute, the valuation put on property exchanged for stock, at a stockholders' meeting, is conclusive on corporate creditors in the absence of fraud.³¹ In North Carolina, where one who paid for stock in property is sued to recover a balance on his subscription it is necessary for defendant to establish that the property was taken in payment at its true value and that such value was approved by a board of directors acting independently in the interests of the corporation, as provided for by statute, in which case if there is no fraud the valuation of the directors is conclusive.³² In Texas, if the secretary of state is satisfied with the value put on the property turned in for stock, and records the charter, his acts as to value are conclusive except in case of fraud.³³ In West Virginia, a corporation may accept property in payment for stock without reference to the actual or market value of the property, in the absence of fraud.³⁴

²⁸ Zierath v. Claggett, — Cal. App. —, 188 Pac. 837.

"Good faith" rule prevails in California. Conley v. Hunt, — Conn. —, 109 Atl. 887.

²⁹ Scully v. Automobile Finance Co., — Del. Ch. —, 109 Atl. 49.

³⁰ John A. Roebling's Sons Co. v. Kinnicutt, 248 Fed. 596.

³¹ Kernan v. Carter, 132 Md. 577, 104 Atl. 530, holding next friend of wife of stockholder was in no better position than creditors.

³² Goodman v. White, 174 N. C. 399, 93 S. E. 906, holding that where board of directors was composed of defendant, his son and another who owned all of the stock of the corporation, the directorate was prejudiced.

³³ Peden Iron & Steel Co. v. Jenkins, — Tex. Civ. App. —, 203 S. W. 180.

³⁴ Taylor v. Citizens' Oil Co., 182 Ky. 350, 206 S. W. 644.

Where two persons purchased a stock of merchandise for less than ten thousand dollars, and immediately incorporated a company with a capital stock of fifty thousand, the merchandise being turned over for all the capital stock, such scheme is a fraud upon prospective creditors of the corporation, and when the corporation is found to be insolvent the stockholders cannot defend a petition by the trustee in bankruptcy to assess the capital stock on the ground that their stock has been fully paid up. The court said that "the referee was right in allowing the value of merchandise as payment on the capital stock, but beyond that the stock was liable to assessment." ³⁵

§ 3577. — Good-will, franchises and other intangibles or prospects. Good-will of a coal business is of no value where the business never made any money in a period of years except in one winter when there was a coal strike.³⁶ If good-will is turned in for stock, the subscriber, when sued by the receiver on his subscription, must show that it had a value equal to the value it was turned in at.³⁷

The cost of mining claims to those who subsequently conveyed them to the corporation for stock is not the test, but the test is the value of such claims to the corporations.³⁸ Prospective earning power of mining claims turned in for stock is not a proper standard of the value of such claims although some evidence of such value.³⁹

§ 3578. — Questions of law and fact; evidence and proof.⁴⁰ Whether stock was issued for full value is a mixed question of law and fact.⁴¹ The burden is on stockholders to prove that property turned in for stock had a cash value equal to the par value of the stock.⁴² The mere fact of failure of a corporation,

³⁵ *In re Phoenix Hardware Co.*, 249 Fed. 410.

³⁶ *Wm. E. Dee Co. v. Proviso Coal Co.*, 290 Ill. 252, 125 N. E. 24, rev'g on other grounds 212 Ill. App. 400.

³⁷ *Hodde v. Hahn*, — Mo. —, 222 S. W. 799.

³⁸ *Clinton Mining & Mineral Co. v. Jamison*, 256 Fed. 577, 582.

³⁹ *Hasson v. Koeberle*, — Cal. —, 181 Pac. 387.

⁴⁰ Evidence admissible on issue as to overvaluation of oil lease turned in for stock, see *Peden Iron & Steel Co. v. Jenkins*, — Tex. Civ. App. —, 203 S. W. 180.

⁴¹ *Sweet v. Barnard*, — Colo. —, 182 Pac. 22.

⁴² *Wm. E. Dee Co. v. Proviso*

as evidenced by a foreclosure, where over ten years after the issue of stock for property, is not of itself evidence of overvaluation of the property.⁴³

§ 3579. Effect of issue, or agreement to issue, watered stock; fraudulent aspect—In general. Watered stock is "void" and cannot be counted in order to constitute a majority of the stock at a stockholders' meeting.⁴⁴ Equity "may declare the unlawful subscription contract to be ineffective to relieve the stockholders of the legal duty to pay the par value of the stock if the interests of the corporation so demand, or it be necessary to do so in order to pay creditors of the company, or if for any reason it be equitable and just to do so."⁴⁵

§ 3581. — Effect in illegal aspect. Stock issued without consideration, in violation of the constitution, as distinguished from stock issued for less than par, is "void."⁴⁶

§ 3583. — Effect as against the corporation. Fraud in overvaluing property turned in to the corporation in payment for stock cannot be set up by the corporation as a set-off in an action against it on notes given for the purchase of its own stock.⁴⁷ A corporation may refuse to perform its contract to deliver stock for services where the value of the services are not equal to the par value of the stock as required by a constitutional provision and statutes; and this is so even though the person seeking specific performance of the agreement to issue stock, offers, pending suit, to pay an additional sum so as to make the price adequate.⁴⁸ A corporation may sue to cancel stock issued by it for a consideration in violation of the statute forbidding issuance of stock except for cash or property.⁴⁹

Coal Co., 290 Ill. 252, 125 N. E. 24, rev'g on other grounds 212 Ill. App. 400.

⁴³ Clinton Mining & Mineral Co. v. Jamison, 256 Fed. 577, 583.

⁴⁴ Bentley v. Zelma Oil Co., 76 Okla. 116, 184 Pac. 131.

⁴⁵ Scully v. Automobile Finance Co., — Del. Ch. —, 109 Atl. 49.

⁴⁶ Lee v. Cameron, — Okla. —, 169 Pac. 17.

⁴⁷ Kelly v. McCormick-Murray Mfg. Co., 201 Ill. App. 308.

⁴⁸ Detroit-Kentucky Coal Co. v. Bickett Coal & Coke Co., 251 Fed. 542, Kentucky case.

⁴⁹ American Macaroni Corporation v. Saumer, — N. Y. Misc. —, 174 N. Y. Supp. 183.

§ 3584. — Effect as against subscribers or purchasers. Stockholders cannot repudiate the issue of stock because of the consideration therefor, where the corporation itself cannot repudiate.⁵⁰ If a corporation sues to cancel stock so far as it exceeds the value of the property turned in for it, the holder cannot elect to pay the balance and hold the excess stock, unless the corporation consents.⁵¹ If stock is issued for property of less value than the face of the stock, and the statute makes fictitious increase of stock void, the holder of such stock may be compelled, at the suit of the corporation or of stockholders suing for it, to surrender so much of the stock as exceeds the value of the property.⁵² A stockholder may recover from corporate officers the amount paid to them for his stock with six per cent interest where the issuance of stock was invalid because the property turned in for stock was not appraised by the Executive Council as required by the statute.⁵³ Where a corporation has no authority to sell stock at less than par, one who purchases from the company at a discount is liable for the amount unpaid thereon.⁵⁴

§ 3585. — Effect as against dissenting stockholders. Dissenting stockholders may enjoin the issuance of watered stock.⁵⁵

§ 3587. — Effect as against subsequent transferees.⁵⁶ A purchaser of stock in good faith from a stockholder, without knowledge that the property given the corporation for the stock was less than its par value, is not subject to the constitutional provision declaring such stock void.⁵⁷ Knowledge of facts which would impel an ordinary careful purchaser of stock to inquire whether it was full paid, is equivalent to actual notice, where an inquiry, if prosecuted, would have shown that the stock was not paid up in that property turned in was overvalued.⁵⁸

⁵⁰ Kunkle v. Soule, — Colo. —, 190 Pac. 536.

⁵¹ Taylor v. Citizens' Oil Co., 182 Ky. 350, 206 S. W. 644, and see § 3583, supra.

⁵² Taylor v. Citizens' Oil Co., 182 Ky. 350, 206 S. W. 644.

⁵³ Fish v. White, — Iowa —, 175 N. W. 748.

⁵⁴ Bank of Ottawa v. Jones, 46

Dom. L. Rep. (Can.) 407.

⁵⁵ Rice v. Thomas, 184 Ky. 168, 211 S. W. 428, quoting Fletcher Cyc. Corp. § 3585.

⁵⁶ See also § 3597, infra.

⁵⁷ Taylor v. Citizens' Oil Co., 182 Ky. 350, 206 S. W. 644.

⁵⁸ In re Manufacturers' Box & Lumber Co., 251 Fed. 957.

§ 3588. Issuance to directors, officers or favored persons. Stock issued to an associated corporation composed of organizers of the first company, for a valueless business idea, is an actual fraud.⁵⁹

§ 3589. Rights of creditors as to water or overvaluation—In general. At common law creditors could not hold stockholders liable on stock which had been issued for property, although the value of the property as agreed upon was greatly in excess of its real value, and such a transaction could be assailed for fraud only.⁶⁰ The prevailing rule at present, however, is that creditors may recover,⁶¹ the right to recover not being an asset of the corporation and hence not inuring to the trustee in bankruptcy, it is often held.⁶² To enforce "a stockholder's liability for unpaid stock issued as full paid, the receiver can only act in the right of creditors."⁶³ The fact that there were no subscriptions in name to the capital stock does not preclude calls on stockholders the same as if they were original sub-

⁵⁹ *Scully v. Automobile Finance Co.*, — Del. Ch. —, 101 Atl. 908.

⁶⁰ *United States Cast Iron Pipe & Foundry Co. v. Henry Vogt Mach. Co.*, 182 Ky. 473, 206 S. W. 806.

⁶¹ If property is taken at an overvaluation, the stockholders are liable to creditors to make up the deficiency. *Wm. E. Dee Co. v. Proviso Coal Co.*, 290 Ill. 252, 125 N. E. 24, rev'g on other grounds 212 Ill. App. 400.

As "between the corporation and the stockholders, the issue of stock for labor which was not performed, and for which no claim was ever presented or allowed by it, may be binding, but not upon creditors seeking to enforce a claim, under the statute, against such stockholders." *Shugart v. Maytag*, — Iowa —, 176 N. W. 886.

Where organizers of a corporation turn in goods for stock, they

are liable for the difference between the value of the goods and the par value of the stock. In re *Phoenix Hardware Co.*, 249 Fed. 410.

Where incorporators who are also subscribers falsely make affidavit that stock is paid for in full, they are liable to creditors, where the amount alleged to have been paid in cash was never in fact paid, and the part of the subscriptions paid in merchandise was paid for at an undervaluation. *Park v. Rich*, — Tex. —, 212 S. W. 947.

Creditors have a right to assume that capital stock issued is of par value. *Rasor v. West Coast Development Co.*, — Ore. —, 192 Pac. 631.

⁶² See § 3598, *infra*.

⁶³ *McDermott v. Woodhouse*, 87 N. J. Eq. 615, 101 Atl. 375, rev'g on other grounds (N. J. Ch.), 99 Atl. 103.

scribers instead of having exchanged a stock of merchandise for the entire capital stock.⁶⁴

Stockholders of mining companies, the same as of other corporations, are liable to creditors for the difference between the price paid for the stock to the corporation and its par value.⁶⁵

Where a creditor holds two judgments against a corporation, and as to one of them he cannot recover against stockholders for the difference between the par value of the stock and the property exchanged for it, voluntary payments by some of the stockholders of their alleged liability for unpaid subscriptions, should not be pro rated between the two judgments but should be applied on the judgment debt for which they could be held liable.⁶⁶

Whether a stockholder of a bankrupt corporation is liable to the estate for the difference between the par value of the stock and the amount originally paid therefor is determined by the law of the state where the company was incorporated.⁶⁷

A stockholder is liable to a creditor of the corporation for the difference between the true value of the property conveyed to the corporation for stock and the par value of the stock, where he dominates and controls the corporation and it has become insolvent; and this is so although he acted in good faith.⁶⁸

§ 3591. — Issue at discount, or for inadequate value, or as bonus. Creditors of an insolvent corporation may recover from stockholders who obtained their stock from the corporation at a price much below its par value, although the

⁶⁴In re Phoenix Hardware Co., 249 Fed. 410.

⁶⁵California Nat. Supply Co. v. Black, — Cal. App. —, 191 Pac. 715.

The rule that if the parties to a transfer of property for stock have put upon the property a valuation in excess of what they know or believe to be its true value, there is a constructive fraud against creditors, and the stock is deemed paid only to the extent of the actual value of the property received in exchange for

it, applies to stock in mining companies as well as in other corporations. Hasson v. Koeberle, 180 Cal. 359, 181 Pac. 387, disapproving contrary rule in In re South Mountain Consol. Min. Co., 14 Fed. 347.

⁶⁶Sherman v. Harley, 178 Cal. 584, 7 A. L. R. 950, 174 Pac. 901.

⁶⁷In re Manufacturers' Box & Lumber Co., 251 Fed. 957.

⁶⁸William E. Dee Co. v. Proviso Coal Co., 212 Ill. App. 400, 403.

stock is issued as fully paid up.⁶⁹ It is elementary that "stockholders, who own stock for which payment has not been made to the corporation, and who are not bona fide holders thereof, are liable to creditors of the corporation for the unpaid balance of the par value of such stock, so far as may be necessary to pay such creditors, notwithstanding that the stock may be fully paid and nonassessable as between the corporation and its stockholders."⁷⁰ Stockholders cannot escape liability to creditors on unpaid subscriptions on the theory that the stock issued to them was void because issued without being paid for and under an agreement that it should not be paid for.⁷¹ In some jurisdictions, however, bonus stock, where directly in violation of constitutional or statutory provisions, is ipso facto invalid so that holders cannot be held liable to creditors as for unpaid stock.⁷²

Holders of common stock are not bona fide purchasers so as to escape liability to creditors for unpaid subscriptions, merely because the contract by which preferred stockholders were to receive common stock as a bonus provided that a certain person should transfer to each purchaser of preferred stock certain common stock as bonus, where the transfer of bonus stock was in fact made by the corporation.⁷³

§ 3593. — As to watered or underpaid increased issues. An alleged increase of stock falsely certified to have been paid in

⁶⁹ California Nat. Supply Co. v. Black, — Cal. App. —, 191 Pac. 715.

⁷⁰ In re Caledonia Coal Co., 254 Fed. 742, 746.

⁷¹ Du Pont v. Ball, — Del. —, 106 Atl. 39, modifying John W. Cooney Co. v. Arlington Hotel Co., — Del. Ch. —, 101 Atl. 879.

⁷² Lavell v. Bullock, — N. D. —, 174 N. W. 764. See Scully v. Automobile Finance Co., — Del. Ch. —, 109 Atl. 49, where common stock issued as bonus to purchasers of preferred stock.

If bonus stock is ipso facto "void" because not issued for money, services or property,

holders are not liable to creditors of the corporation for the amount due on the stock. Lavell v. Bullock, — N. D. —, 174 N. W. 764.

In California, one who receives stock without consideration, in violation of constitutional and statutory provisions forbidding issuance of stock except for money, etc., is not liable to creditors as for an unpaid subscription, on the theory that such stock is void. J. F. Lucey Co. v. McMullen, 178 Cal. 425, 173 Pac. 1000.

⁷³ Stoecker v. Goodman, 183 Ky. 330, 209 S. W. 374.

in full when in fact nothing was paid thereon, in violation of a statute forbidding increase of stock except for money paid, labor done or property received, is illegal and void.⁷⁴ Where a corporation, after engaging in business for some time, issues stock as a bonus but as fully paid up, to one lending it money to pay pressing obligations, and the bonus stock when issued had no actual market value, the holder of such stock is not liable to creditors for the amount unpaid on it, in the absence of fraud, where the stock was not shown to have any greater value when issued than the consideration for which issued.⁷⁵

§ 3595. — Antecedent creditors and creditors with notice or assenting.⁷⁶ If one deals with a corporation with knowledge that stock was issued without being paid for, he cannot recover against stockholders as for unpaid subscriptions.⁷⁷ A creditor of a corporation who knows when he becomes such that its shares of stock have been issued to the subscribers therefor without payment of money or money's worth, cannot enforce his claim against such shareholders to the extent of their indebtedness for the stock issued to them; but subsequent knowledge is no bar.⁷⁸ But it has been held in Delaware that liability to creditors on unpaid subscriptions is not affected by knowledge of the creditors of the facts under which the common stock was issued, and this is so even as to creditors actually participating in the issuance of unpaid stock as full paid.⁷⁹ Where one extends

⁷⁴ Hess Warming & Ventilating Co. v. Burlington Grain Elevator Co., — Mo. —, 217 S. W. 493.

⁷⁵ J. F. Lucey Co. v. McMullen, 178 Cal. 425, 173 Pac. 1000.

⁷⁶ Defense to action by creditor against stockholder to recover amount unpaid on stock, that the creditor did not rely on the apparent amount of outstanding capital stock when he contracted with it, held not supported by the evidence in *Keyes v. Baskerville*, — S. D. —, 175 N. W. 874, citing *Fletcher Cye. Corp.* § 3595.

⁷⁷ *Watt v. German Sav. Bank*, 183 Iowa 346, 165 N. W. 897.

But a creditor who is also a director is entitled to share in a recovery against common stockholders for the unpaid balance on their stock, although he extended credit to the company with full knowledge that the common stock was issued as a bonus to subscribers to the preferred stock. *Stoecker v. Goodman*, 183 Ky. 330, 209 S. W. 374, explaining *Miller v. Higginbotham's Adm'r*, 29 Ky. L. Rep. 549, 93 S. W. 655.

⁷⁸ *Scott v. Luehrmann*, 278 Mo. 638, 213 S. W. 855.

⁷⁹ *Du Pont v. Ball*, — Del. —, 106 Atl. 39, modifying *John W.*

credit to a corporation with knowledge that stock was exchanged for property worth less than the par value of the stock, such creditor cannot hold stockholders liable for the overvaluation.⁸⁰ A trustee in bankruptcy cannot recover from stockholders because of issuance of stock in exchange for property at an overvaluation, in favor of creditors who became such with knowledge of the facts.⁸¹ Corporation creditors who became such prior to cancellation by the company of bonus stock issued by it cannot collect on the stock as unpaid stock nor attack its cancellation, where their debts are not yet due and the corporation is not insolvent.⁸²

§ 3596. Measure and extent of liability to creditors—In general. If stock is issued below par, the judgment against the stockholder should be for the difference between the par value and the amount paid, together with interest from the time when the stock was issued.⁸³ If property is turned in as payment for stock, the stockholder is liable as for unpaid subscription to the amount of difference between the real value of the property turned in and the par value of the stock.⁸⁴ In Delaware, however, it is held that damages for fraud of directors and promoters in selling property to the company in exchange for stock is the difference between the market value (not the par value) of the stock issued and the value of the property received.⁸⁵ Where there is some consideration for stock issued for services grossly overvalued, the court may credit the holder for the actual value of the services, when sued for the balance due.⁸⁶

An assessment is necessary before a stockholder in a bank-

Cooney Co. v. Arlington Hotel Co., — Del. Ch. —, 101 Atl. 879, and explaining cases to contrary.

⁸⁰ Sherman v. Harley, 178 Cal. 584, 7 A. L. R. 950, 174 Pac. 901; Baldwin v. Timber Inv. Co., — N. D. —, 176 N. W. 662.

⁸¹ Courtney v. Youngs, 201 Mich. 384, 168 N. W. 441.

⁸² Rice v. Thomas, 184 Ky. 168, 211 S. W. 428.

Creditors who become such after cancellation of certain bonus

stock cannot object to such cancellation nor collect on the stock as unpaid stock. Rice v. Thomas, 184 Ky. 168, 211 S. W. 428.

⁸³ Whitewater Tile & Pressed Brick Mfg. Co. v. Johnson, — Wis. —, 175 N. W. 786.

⁸⁴ Jones v. Bowman, 181 Ky. 722, 205 S. W. 923.

⁸⁵ Du Pont v. United Oil & Fuel Co., — Del. Ch. —, 109 Atl. 136.

⁸⁶ Scully v. Automobile Finance Co., — Del. Ch. —, 109 Atl. 49.

rupt corporation can be held liable for the difference between the value of property turned in for stock and the par value of the stock.⁸⁷

§ 3597. — Effect of transfer on liability to creditors.⁸⁸ A purchaser of stock, originally issued as paid up in exchange for fraudulently overvalued property, is not liable to corporate creditors for the unpaid balance of its par value in excess of the true value of the property, where he acquired the stock in good faith and without notice.⁸⁹ A creditor seeking to hold a transferee of stock for unpaid balances, or the par value in excess of the value of property exchanged therefor, must show that he is not a holder in good faith without notice that the stock had not been fully paid for.⁹⁰ A subscriber to stock compelled to pay the difference between the value of property turned in for stock and the par value of the stock, at the suit of a corporate creditor, has no cause of action against his transferee of the stock to recover such payment.⁹¹ In construing the North Dakota statutes making stockholders liable to creditors for the amount unpaid on the stock, it is held that "a bona fide transferee of stock which has been sold to him as fully paid is not liable for any portion of the unpaid subscription or for any difference there may be between the par value and the amount received by the corporation at the time the stock was originally issued."⁹²

§ 3598. Remedies and procedure.⁹³ Where a trustee in bankruptcy of a corporation sues to recover of a stockholder because his stock was issued in exchange for property at an overvaluation, the suit must be in equity and not on the law side.⁹⁴

⁸⁷ *In re Manufacturers' Box & Lumber Co.*, 251 Fed. 957.

⁸⁸ See also § 3587, *supra*.

⁸⁹ *Feehan v. Kendrick*, 32 Idaho 220, 179 Pac. 507.

⁹⁰ *Smoot v. Larsen*, — Idaho —, 189 Pac. 1105.

⁹¹ *Jones v. Bowman*, 181 Ky. 722, 205 S. W. 923.

⁹² Opinion of Judges Birdzell and Hanley concurring specially

in *Lavell v. Bullock*, — N. D. —, 174 N. W. 764, citing *Fletcher Cyc. Corp.* § 3771, and referring to Illinois and Washington decisions in support of rule.

⁹³ This section of *Fletcher* is quoted in *Rice v. Thomas*, 184 Ky. 168, 211 S. W. 428.

⁹⁴ *Courtney v. Youngs*, 202 Mich. 384, 168 N. W. 441.

Where stock is issued for labor grossly overvalued, equity may give the holder credit in some way for the real consideration, as by allowing the real value of the services.⁹⁵ Where all the holders of common stock took their shares with notice that they were bonus or gratuity shares, for which they paid nothing, or else they were put on inquiry, such stock should not be cancelled but it should be held to be assessable and each share should be made to show what has been paid or credited thereon.⁹⁶

A trustee in bankruptcy of a corporation cannot enforce, for the benefit of creditors, the difference between the real value of property turned in for stock and its par value, since not an asset of the corporation.⁹⁷ A trustee in bankruptcy cannot enforce the New York statutory remedy where the property turned in for stock is inadequate and the transaction is coupled with fraud, since the statutory remedy is given only to creditors and not to the corporation.⁹⁸ One who becomes a creditor after the issuance of stock for overvalued property is entitled to recover the difference between the real value of the property and the par value of the stock, where the corporation becomes insolvent, and the right to sue is in such creditors rather than the trustee in bankruptcy of the corporation.⁹⁹

A complaint in an action by creditors is insufficient where it does not allege that the stock was not fully paid at the time the action was begun—it not being sufficient to merely allege that the stock was issued without consideration.¹

Limitations do not begin to run against an action by a trustee in bankruptcy against stockholders because of issuance of stock

⁹⁵ *Scully v. Automobile Finance Co.*, — Del. Ch. —, 109 Atl. 49.

⁹⁶ *Scully v. Automobile Finance Co.*, — Del. Ch. —, 109 Atl. 49.

⁹⁷ *State Bank of Commerce v. Kenney Band Instrument Co.*, 143 Minn. 236, 173 N. W. 561. Contra, see *Grand Rapids Trust Co. v. Nichols*, 199 Mich. 126, 165 N. W. 667.

Right of trustee in bankruptcy of insolvent corporation to sue in equity, see *Porter v. Hughes*, 198 Ala. 36, 73 So. 400.

Limitations on power of trustee in bankruptcy of a corporation to sue stockholder because of issuance of stock for overvalued property, see *Courtney v. Youngs*, 201 Mich. 384, 168 N. W. 441.

⁹⁸ *In re Berler Shoe Co.*, 246 Fed. 1018.

⁹⁹ *State Bank of Commerce v. Kenney Band Instrument Co.*, 143 Minn. 236, 173 N. W. 561.

¹ *Graeber v. Ehrigott*, 182 N. Y. App. Div. 377, 169 N. Y. Supp. 32.

in exchange for property at an overvaluation, until the order of the referee in bankruptcy requiring payments on such stock.²

Proof of an arrangement as to issuance of stock for property, and the acquiescence of stockholders therein, is admissible, although not in fact entered on the minutes, so long as it does not contradict the minutes.³

XIII. LIEN OF CORPORATION ON SHARES

§ 3599. In the absence of express provisions or agreement.

A corporation has no lien on its stock for debts owing it by the stockholder in the absence of a provision therefor in the charter, a statute or by-law, or an agreement.⁴

§ 3601. Liens under by-laws.⁵

§ 3608. Debts for which lien attaches—Debts contracted after transfer. The lien in favor of a corporation on its stock does not attach, as against a transferee, where the president and nearly all the directors had knowledge of the transfer prior to the creation of the debt in its favor against the original holder.⁶

§ 3620. Waiver or estoppel to assert lien. Corporate lien on stock is not waived by taking other security for a loan to a stockholder.⁷ A corporation is not estopped to claim a lien on its stock by failure to protest when a pledgee stated he was informed by a corporate officer that the corporation had no claims against the stock, where no detriment resulted from the statement.⁸ A person is not an innocent purchaser of stock, as against the lien of the corporation on such stock, because of a letter from the corporation stating that it had no claims against

² Courtney v. Youngs, 201 Mich. 384, 168 N. W. 441.

³ East Lake Lumber Co. v. Van Gorder, 105 N. Y. Misc. 704, 174 N. Y. Supp. 38.

⁴ Damron v. Denny, 149 Ga. 280, 99 S. E. 851, citing Fletcher Cyc. Corp. § 3599; Lask v. Bedell (N. J. Ch.), 109 Atl. 849.

⁵ Notice of, see § 515, supra.

Note on "validity and effect of

provision in charter, statute or by-law creating lien on stock in favor of corporation," see Ann. Cas. 1918 D 368.

⁶ Bank of Norwood v. Ray, 21 Ga. App. 620, 94 S. E. 819.

⁷ Wight v. Washoe County Bank, 251 Fed. 819.

⁸ Mobile Towing & Wrecking Co. v. First Nat. Bank of Lakeland, 201 Ala. 419, 78 So. 797.

the stock, where the letter is not shown to have been written at a time when it induced action to the detriment of the purchaser.⁹ Failure to give notice of the corporation's lien on stock, with knowledge that one dealing with the stockholder relies on his ownership, makes the lien inferior to the creditor making advances to the stockholder on the faith of such ownership.¹⁰ Delay in enforcing a corporate lien on stock does not affect the lien as against the real owner of the stock, where the corporation had no knowledge that the stock was not owned by the apparent owner.¹¹

XIV. PREFERRED STOCK

§ 3621. Definition, nature and distinctions. Ordinarily stock is said to be preferred when it is entitled to dividends from the earnings or income of the corporation before any other dividends are paid.¹² The designation of stock as preferred does not make it such nor define the rights of the holder thereunder.¹³ A certificate of indebtedness is quite a different thing from a certificate of stock.¹⁴

§ 3622. Power to issue preferred or guaranteed stock—In general.¹⁵ In the absence of statutory provision to the contrary, the certificate of incorporation of a business corporation may make such preferences between stockholders as to its stock as seems best.¹⁶

§ 3625. — Extent of power. By unanimous consent of stockholders, new preferred stock may be issued to be placed ahead of the old preferred and redeemable above par or convertible into common.¹⁷ The issuance of new preferred stock to be placed

⁹ *Mobile Towing & Wrecking Co. v. First Nat. Bank of Lakeland, Florida*, 201 Ala. 419, 78 So. 797.

¹⁰ *Lazard Bros. & Co. v. Union Bank of Canada*, 51 Dom. L. Rep. (Can.) 636.

¹¹ *Wight v. Washoe County Bank*, 251 Fed. 819.

¹² *Wright v. Johnston*, 183 Iowa 807, 167 N. W. 680.

¹³ *Wright v. Johnston*, 183 Iowa 807, 167 N. W. 680.

¹⁴ *Armstrong v. Union Trust & S. Bank*, 248 Fed. 268.

¹⁵ As stock dividend, see § 3682, *infra*.

¹⁶ *People v. Hugo*, 191 N. Y. App. Div. 628, 182 N. Y. Supp. 9.

¹⁷ *General Inv. Co. v. Bethlehem Steel Corporation*, 88 N. J. Eq. 237, 102 Atl. 252.

ahead of existing preferred stock and convertible into common stock without pre-emptive rights may be authorized by, unanimous consent of the stockholders, or they may be estopped to attack the validity of the issue.¹⁸

In Alabama the statute authorizes the issuance of preferred stock "in no case exceeding two-thirds of the capital stock paid for in cash or property";¹⁹ and this means two-thirds of the common stock.²⁰

§ 3628. Preferred stockholders as creditors—General rule. Ordinarily, holders of preferred stock are not corporate creditors,²¹ until a dividend is declared;²² and they are not creditors because of dividends in arrears where no dividends have been declared by the directors.²³ Preferred stock may itself provide for payment at par with interest, on surrender at the expiration of two years, so as to make one tendering his certificate at the end of the two years a general creditor.²⁴

§ 3630. — Relation both as stockholders and creditors. Where preferred stock makes the holders assured of dividends, gives them a right to compel repayment of the par value of the stock, and precludes them from voting or sharing in any surplus, it creates the relation of creditor and debtor, and the stock is void as stock.²⁵

§ 3631. — Construction and effect of contract. Certificates reciting that the holder is entitled to interest on the par value thereof, where the holders expect to share in dividends, make the holders stockholders and not creditors, although the cor-

¹⁸ General Inv. Co. v. Bethlehem Steel Corporation, 88 N. J. Eq. 237, 102 Atl. 252.

¹⁹ Heide v. Capital Securities Co., 200 Ala. 397, 76 So. 313, holding the issuance of \$100,000 preferred stock which had for its basis only \$1,000 in cash was a violation of the statute.

²⁰ Citizens' Loan & Savings Co. v. Arwood, — Ala. App. —, 81 So. 854.

²¹ Armstrong v. Union Trust & Savings Bank, 248 Fed. 268.

²² Wilder v. Trefry, — Mass. —, 125 N. E. 689.

²³ Wilder v. Trefry, — Mass. —, 125 N. E. 689.

²⁴ Allen v. Northwestern Mfg. Co., — Iowa —, 179 N. W. 130. But see § 3630, *infra*.

²⁵ Wright v. Johnston, 183 Iowa 807, 167 N. W. 680. Compare § 3629, *supra*.

poration, reserves the right to retire the certificates on certain conditions specified, and it agrees to redeem "said stock" at par, with accrued interest.²⁶ An agreement to redeem so-called preferred stock at the end of a certain number of years does not create the relation of lender and borrower but makes the person a preferred stockholder where the stock he receives is otherwise about the same as ordinary preferred stock.²⁷

§ 3632. Rights and remedies of preferred stockholders—In general. Preferred stock may be given a superior lien on the corporate property as against common stock.²⁸

§ 3634. — Rights subordinate to those of creditors. A corporation cannot, in the absence of statutory authority, make its preferred stock a lien upon its property so as to give a priority against general creditors.²⁹ Unless a statute authorizes it, preferred stock cannot be issued so as to give the holders priority, by virtue of a mortgage, and a right to compel redemption, over general creditors.³⁰ Including conditions in preferred stock which tend to impair the corporate capital available for the satisfaction of creditors makes the certificates void as stock.³¹

§ 3639. — Rights on increase or reduction of capital stock.³²

§ 3642. Rights of common stockholders with respect to preferred stock. A provision giving preferred stockholders priority for repayment of their capital in a winding up does not negative their ordinary right as corporators to participate in surplus assets.³³

²⁶ *Armstrong v. Union Trust & Savings Bank*, 248 Fed. 268.

²⁷ *Booth v. Union Fibre Co.*, 142 Minn. 127, 171 N. W. 307.

²⁸ *Hewitt v. Linnhaven Orchard Co.*, 90 Ore. 1, 174 Pac. 616.

²⁹ *Hewitt v. Linnhaven Orchard Co.*, 90 Ore. 1, 174 Pac. 616.

³⁰ An agreement to secure preferred stockholders, so that their claims will be prior to the gen-

eral indebtedness of the corporation, is against public policy and void as to subsequent creditors. *Hewitt v. Linnhaven Orchard Co.*, 90 Ore. 1, 174 Pac. 616.

³¹ *Wright v. Johnston*, 183 Iowa 807, 167 N. W. 680.

³² See generally § 3642 et seq., *infra*.

³³ *In re Frazer and Chalmers, Ltd.*, [1919] 2 Ch. Div. 114.

§ 3643. Exchange of preferred stock for common stock, or common stock for preferred.³⁴

§ 3645. Redemption and retirement—Right of stockholders to compel redemption. Statutory restrictions on payments to stockholders where the assets are not sufficient to pay creditors do not preclude a redemption of preferred stock as per agreement at the time of its issuance.³⁵ But it is held that a corporation cannot be compelled to redeem preferred stock as per its agreement, where it is insolvent, although it is not in liquidation and no creditor is asking relief.³⁶

XV. CONVERTIBLE STOCK

§ 3648. Exchange of stock for bonds or property. Where stock is purchased with partnership funds, with the knowledge of the corporation, and a certificate is issued in the name of one of the partners, he and not the partnership, is the holder of the stock within a provision that each "holder" of preferred stock "may retire the same at 33½% per annum in the products of the company at current prices."³⁷

XVI. DIVIDENDS

§ 3649. Definition and nature of dividends.³⁸ The assets of a dissolved corporation are not distributed as dividends, as dividends are commonly known.³⁹

§ 3650. Dividends distinguished from profits. "Dividends" and "profits" are ordinarily different things.⁴⁰ Profits are the surplus earnings available for the payment of dividends.⁴¹

³⁴ Power to create a preferred stock convertible into common, see *General Inv. Co. v. Bethlehem Steel Corporation*, 88 N. J. Eq. 237, 102 Atl. 252.

³⁵ *Allen v. Northwestern Mfg. Co.*, — Iowa —, 179 N. W. 130.

³⁶ *Booth v. Union Fibre Co.*, 142 Minn. 127, 171 N. W. 307.

³⁷ *National Sewer Pipe Co. v. Smith-Jaycox Lumber Co.*, 183 Iowa 17, 166 N. W. 708, holding that firm could not exercise such option.

³⁸ Other definitions, see *Wilder v. Trefry*, — Mass. —, 125 N. E. 689; *Rossi v. Rex Consol. Min. Co.*, 108 Wash. 296, 183 Pac. 120.

What constitutes a dividend within the Income Tax Law, see *Wilder v. Trefry*, — Mass. —, 125 N. E. 689, and see § 4659, *infra*.

³⁹ *Rossi v. Rex Consol. Min. Co.*, 108 Wash. 296, 183 Pac. 120.

⁴⁰ *Warfield v. Kelly*, 262 Pa. 482, 106 Atl. 72.

⁴¹ *Cochrane v. Interstate Pack-*

§ 3652. Stockholders' right to share in profits—Rights before dividend is declared. Stockholders are not entitled to dividends until the directors in their discretion declare a dividend.⁴² No action lies to recover a dividend until the dividend has been declared.⁴³ But contractual rights of stockholders to dividends, as evidenced by the articles of incorporation and the statutes in force when the corporation was created, cannot be abrogated by changing the corporation to a co-operative association.⁴⁴

§ 3656. Compelling declaration and paying of dividends—In general.⁴⁵ While directors may be compelled to declare a dividend where they fraudulently or arbitrarily refuse to do so,⁴⁶ a court will require directors to declare a dividend only "upon clear and satisfactory proof of the company's ability to pay a substantial dividend on its capital stock after making reasonable provision for its present obligations and anticipated needs for a reasonable time in the future."⁴⁷ They will not be compelled to declare dividends unless there is bad faith or an abuse of discretion.⁴⁸ A contract between stockholders will not be construed so as to compel directors to declare dividends annually, regardless of the best interests of the company, unless its terms are explicit.⁴⁹

Minority stockholders are not estopped to demand larger dividends because they had acquiesced in an increase of the capital stock from two to one hundred million by a stock dividend.⁵⁰

ing Co., 139 Minn. 452, 167 N. W. 111.

⁴² *Southern Pac. Co. v. Lowe*, 247 U. S. 330, 62 L. Ed. 1142, rev'g on other grounds 238 Fed. 847.

⁴³ *Castorland Milk & Cheese Co. v. Shantz*, 179 N. Y. Supp. 131.

⁴⁴ *Allen v. White*, 103 Neb. 256, 171 N. W. 52.

⁴⁵ For article on power of courts to compel declaration of dividend, see 3 *Southern Law Quarterly* 281-292.

⁴⁶ *Baillie v. Columbia Gold Min. Co.*, 86 Ore. 1, 167 Pac. 1167.

⁴⁷ *Bickel v. Henry Bickel Co.*, 184 Ky. 582, 212 S. W. 602.

⁴⁸ *Pardee v. Harwood Elec. Co.*, 262 Pa. 68, 105 Atl. 48.

In case of doubt as to the propriety of declaring a dividend, the directors should not declare the dividend. *Bickel v. Henry Bickel Co.*, 184 Ky. 582, 212 S. W. 602.

A public service corporation should not declare such dividends as will destroy or impair its efficiency. *Pardee v. Harwood Elec. Co.*, 262 Pa. 68, 105 Atl. 48.

⁴⁹ *De Jonge v. Zentgraf*, 182 N. Y. App. Div. 43, 169 N. Y. Supp. 377.

⁵⁰ *Dodge v. Ford Motor Co.*, 204 Mich. 459, 170 N. W. 668.

A Michigan case given much space in the newspapers was an action by the Dodge brothers to compel the Ford Motor Company to declare a larger dividend. The facts were that the company had assets of more than \$132,000,000, a surplus of almost \$112,000,000, its cash on hand and municipal bonds were nearly \$54,000,000, its total liabilities including capital stock were a little over \$20,000,000, and no extra dividend had been declared during the business year although it had been the practice under similar circumstances to declare larger dividends. The profits for the preceding year were \$59,000,000, and the directors had refused to declare a dividend of more than \$1,200,000. As an excuse for not declaring larger dividends, the Ford company declared its intention of enlarging the plant, not to make more money but to enable it to sell its cars cheaper, but the supreme court held that benefiting the public should not be the primary purpose of a business corporation, and where the proposed improvements would not exceed \$24,000,000, and the yearly profits were around \$60,000,000, it was proper to require the declaration of an extra dividend of \$19,000,000.⁵¹

§ 3657. — Jurisdiction and procedure.⁵² A demand on the directors to declare a dividend is a condition precedent to the right to sue to compel them to declare a dividend.⁵³ The remedy to compel declaration of dividends is by a suit in equity and not by an action at law.⁵⁴

§ 3658. Dividends payable out of profits only—General rule.⁵⁵ Where the rights of no creditors are involved, and the company is solvent, a corporation cannot defend an action to recover a dividend on the ground that the dividend declared was in excess of the net profits.⁵⁶

⁵¹ Dodge v. Ford Motor Co., 204 Mich. 459, 170 N. W. 668.

⁵² Sufficiency of complaint in action to compel declaration of dividends, see Bickel v. Henry Bickel Co., 184 Ky. 582, 212 S. W. 602.

⁵³ Bickel v. Henry Bickel Co., 184 Ky. 582, 212 S. W. 602.

⁵⁴ De Jonge v. Zentgraf, 182 N. Y. App. Div. 43, 169 N. Y. Supp. 377.

⁵⁵ See also § 3659, *infra*.

⁵⁶ Thiry v. Banner Window Glass Co., 81 W. Va. 39, L. R. A. 1918 B 1048, 93 S. E. 958.

§ 3659. — Unconditional agreement to pay dividends. An agreement to pay dividends must be read in connection with a statute forbidding the declaration of dividends except from surplus profits.⁵⁷ A contract with preferred stockholders of a public service corporation, requiring the payment of dividends, where it would lessen the efficiency of the corporation to serve the public, is invalid.⁵⁸

§ 3660. Determination of profits—In general. The fact that certain balances are denominated, in the corporate books, as net earnings, is, as against the corporation, persuasive but not conclusive evidence that they are such.⁵⁹

§ 3661. — Time of determining profits. In determining whether notes or accounts are properly included in the assets, their value at the time the dividend was declared rather than at a subsequent time is the test.⁶⁰ Common stockholders cannot claim reimbursement for dividends in former years when no profits were earned, as against preferred stock, since dividends are not cumulative without an express or implied agreement to that effect.⁶¹

§ 3664. — Money due but not received. Book accounts concerning which there is no question may be included in the assets of a corporation in determining whether there has been a net profit.⁶²

§ 3666. — Creation of reserve fund for repairs, etc. In determining whether there are profits, where the property of a constituent coal company is being rapidly exhausted by the consolidated company, it is proper to set aside a sinking fund to cover the exhaustion for several years back.⁶³

⁵⁷ *Castorland Milk & Cheese Co. v. Shantz*, 179 N. Y. Supp. 131.

⁵⁸ *Pardee v. Harwood Elec. Co.*, 262 Pa. 68, 105 Atl. 48.

⁵⁹ *Pardee v. Harwood Elec. Co.*, 262 Pa. 68, 105 Atl. 48.

⁶⁰ *Quinn v. Quinn Mfg. Co.*, 201 Mich. 664, 167 N. W. 898.

⁶¹ *Englander v. Osborne*, 261 Pa. 366, 6 A. L. R. 800, 104 Atl. 614.

⁶² *Quinn v. Quinn Mfg. Co.*, 201 Mich. 664, 167 N. W. 898.

⁶³ *Pardee v. Harwood Elec. Co.*, 262 Pa. 68, 105 Atl. 48.

§ 3667. — Valuation of property. Mere estimates of increased value of property do not constitute profits from which dividends may be declared.⁶⁴

§ 3668. — Property or money representing capital stock.⁶⁵ A manufacturing corporation may set off losses incurred in business in preceding years against a bona fide valuation of appreciation of the assets of the corporation, and declare a dividend out of the profits of the business in succeeding years.⁶⁶ A surplus which existed from the time of a merger cannot be regarded as net earnings for dividend purposes.⁶⁷

§ 3670. — Corporations whose property is necessarily consumed in use.⁶⁸

§ 3671. — Further illustrations. Dividends may be paid out of premiums paid for stock, i. e., the amounts paid above par.⁶⁹ But it is held in California that proceeds of sales by a corporation of its own stock, even when sold for more than par value, are part of the original assets or capital stock, and are not profits which may be distributed as dividends.⁷⁰

§ 3672. In whom authority to declare dividends is vested.⁷¹ Generally only directors can declare dividends.⁷² But where all the stock is owned by two persons, except one share, the beneficial interest in which was in one of them, dividends cannot be recovered by the trustee in bankruptcy because paid without any vote of the directors, where the corporation was solvent at the time.⁷³ So where the rights of no creditors are involved,

⁶⁴ *Southern California Home Builders v. Young*, — Cal. App. —, 188 Pac. 586.

⁶⁵ See § 3671, *infra*.

⁶⁶ *Ammonia Soda Co., Ltd. v. Chamberlain*, [1918] 1 Ch. Div. 266.

⁶⁷ *Pardee v. Harwood Elec. Co.*, 262 Pa. 68, 105 Atl. 48.

⁶⁸ See § 3666, *supra*.

⁶⁹ *Smith v. Cotting*, 231 Mass. 42, 120 N. E. 177.

⁷⁰ *Merchants' & Insurers' Reporting Co. v. Schroeder*, 39 Cal. App. 226, 178 Pac. 540.

⁷¹ For note on "declaration of dividends by stockholders," see L. R. A. 1918 B 1051.

⁷² *Cuppy v. Ward*, 187 N. Y. App. Div. 625, 176 N. Y. Supp. 233.

⁷³ *Atherton v. Beaman*, 264 Fed. 878.

the corporation is bound by the declaration of a dividend by the stockholders instead of the directors, where, by common consent, stockholders and directors concur in the management and control of the corporation.⁷⁴

§ 3673. Formal requisites of declaration. The fact that directors declare dividends at a meeting called a stockholders' meeting, instead of at a directors' meeting, is not fatal.⁷⁵ Where creditors are not affected or injured through a division of a corporation's surplus among its stockholders, there is no necessity for a formal declaration of dividends.⁷⁶ Where directors also constituted all the stockholders, they can distribute surplus without going through the form of declaring a dividend.⁷⁷ Where stockholders agreed that fifty per cent of the profits was to be distributed, and the other fifty left in the business and credited to the profit account of the respective stockholders, the reserved profits should be distributed among the parties to the contract at its expiration.⁷⁸

Acquiescence by all the stockholders for over five years in a division of surplus among the stockholders estops the corporation to attack such division because of informalities relating thereto.⁷⁹

§ 3674. Discrimination between stockholders. The right of stockholders to pro rata dividends the same as other stockholders cannot be divested by arbitrary action of directors or stockholders attempting to classify stockholders.⁸⁰ But a co-operative corporation may fix a dividend of seven per cent and a division of the balance among stockholders pro rata according to the "amount of business each has furnished to the company during the year," in the form of furnishing to it the product or products in which it is dealing.⁸¹

⁷⁴ *Thiry v. Banner Window Glass Co.*, 81 W. Va. 39, L. R. A. 1918 B 1048, 93 S. E. 958.

⁷⁵ *Quinn v. Quinn Mfg. Co.*, 201 Mich. 664, 167 N. W. 898.

⁷⁶ *Freeman v. Rogers White Lime Co.*, 138 Ark. 312, 211 S. W. 146.

⁷⁷ *Griffin v. Brody, Adler & Koch Co.*, 167 N. Y. Supp. 725.

⁷⁸ *Bernstein v. Esskay Waist Co.*, 176 N. Y. Supp. 94.

⁷⁹ *Freeman v. Rogers White Lime Co.*, 138 Ark. 312, 211 S. W. 146.

⁸⁰ *Thiry v. Banner Window Glass Co.*, 81 W. Va. 39, L. R. A. 1918 B 1048, 93 S. E. 958.

⁸¹ *Mooney v. Farmers' Mercantile & Elevator Co.*, 138 Minn. 199,

§ 3677. Cash dividends. A dividend is not a mere form where separate warrants are sent to stockholders, respectively entitled extra dividend warrant and stock subscription warrant, with the option to indorse the latter if it was desired to take stock or to use the dividend warrant if cash was preferred.⁸²

If all the stockholders consent thereto, they may distribute certain of the assets among the stockholders, such as stock held in another company.⁸³ If stock of another company has been distributed among the stockholders under a mistake of law as to the effect thereof, and such stock was purchased so as to control a supply of raw wool, a nonratifying stockholder may obtain relief in equity by having the distribution set aside.⁸⁴

§ 3681. Stock dividends—General principles.⁸⁵ "All dividends," as used in a contract, includes stock dividends.⁸⁶ Preferred stock issued to a stockholder, to represent profits undrawn, is valid where approved by all the directors and stockholders.⁸⁷ In some states, trust companies are expressly prohibited by statute from declaring stock dividends.⁸⁸

§ 3683. — Necessity for surplus profits. The fact that a cash dividend in the same amount as a stock dividend could not have been paid without borrowing money does not show that the stock dividend represents capital increase rather than profits.⁸⁹

§ 3684. — Effect of stock dividends.⁹⁰

164 N. W. 804, holding that former custom of distributing all the surplus to all stockholders alike was no bar.

⁸² *Smith v. Cotting*, 231 Mass. 42, 120 N. E. 177.

⁸³ *Hoberg v. John Hoberg Co.*, 170 Wis. 50, 173 N. W. 639.

⁸⁴ *Hoberg v. John Hoberg Co.*, 170 Wis. 50, 173 N. W. 639.

⁸⁵ Nature of stock dividends, see *Palmer v. Pullman Co.*, 252 Fed. 286; *Security Trust Co. v. Rammelsburg*, 82 W. Va. 701, 97 S. E. 122.

Stock dividend held a distribution of profits rather than in-

crease in value, see *Sexton v. C. L. Percival Co.*, — Iowa —, 177 N. W. 83.

Stock dividends as subject to federal income tax, see § 4659 et seq., *infra*.

⁸⁶ *Sexton v. C. L. Percival Co.*, — Iowa —, 177 N. W. 83.

⁸⁷ *Beaman v. Gerrish*, — Mass. —, 126 N. F. 352.

⁸⁸ *Smith v. Cotting*, 231 Mass. 42, 120 N. E. 177.

⁸⁹ *Sexton v. C. L. Percival Co.*, — Iowa —, 177 N. W. 83.

⁹⁰ Income tax, see § 4659 et seq., *infra*.

§ 3687. Remedies of stockholders to recover dividends—Action at law against corporation.⁹¹

§ 3693. — Statute of limitations. An action by the United States to recover dividends is not brought as a stockholder, so as to be bound as a private person by statutes and rules of limitation, but as a creditor.⁹²

§ 3699. Persons entitled to dividends in general. Where one holds stock under a contract entitling him to all dividends but authorizing another to repurchase it at par, on the holder's death, the former is entitled to a stock dividend if it is a distribution of profits but not where it merely represents increase in value of the corporation's investment.⁹³

§ 3700. Rights on transfer of stock—General rule. Dividends belong to the holder of stock at the time they are declared, although the stock is sold before the dividends are paid, unless the dividends are expressly included in the sale.⁹⁴

§ 3701. — Executory contracts to sell; sales for future delivery.⁹⁵ Dividends declared while a contract to sell stock is executory belong to the purchaser and not to the seller, in absence of any agreement in regard thereto, it is held in Nebraska.⁹⁶ If the stock is sold to be paid for by services to be performed in the future, the buyer is entitled to dividends after such sale although the stock certificates are not delivered until after full performance of the services.⁹⁷

Dividends accruing while a contract for sale of stock is in escrow, where there is no express agreement as to the dividends,

⁹¹ Admissibility of evidence in action to recover dividends declared, see *Privat v. Grand Bay Land Co.*, 41 S. D. 494, 171 N. W. 327.

⁹² *Chesapeake & Delaware Canal Co. v. United States*, 250 U. S. 123, 63 L. Ed. 889, aff'g 240 Fed. 903.

⁹³ *Sexton v. C. L. Percival Co.*, — Iowa —, 177 N. W. 83.

⁹⁴ *Western Securities Co. v. Sil-*

ver King Consol. Min. Co. of Utah, — Utah —, 192 Pac. 664.

⁹⁵ For note on right to dividend declared between the making of a contract for the sale of stock and the delivery of the stock, see L. R. A. 1917 F 553.

⁹⁶ *Bank of Waverly v. Daily*, 103 Neb. 7, 170 N. W. 183.

⁹⁷ *Hubbard v. George*, 81 W. Va. 538, L. R. A. 1918 C 835, 94 S. E. 974.

belong to the purchaser.⁹⁸ Where a certain number of shares of stock were placed in escrow, to be delivered when payment of a specific sum had been made therefor out of future declared dividends, no recovery of dividends can be had by the person in whose favor the stock was placed in escrow where he was not entitled to delivery because payment of the agreed sum had not been made.⁹⁹

§ 3702. — Provisions of statute, charter or by-laws. Where a by-law of a co-operative warehouse company imposes, as a condition to the right to participate in dividends, the necessity for being a stockholder in the corporation, one who sells his stock cannot reserve the right to future dividends so as to be entitled thereto.¹

§ 3703. — Contract modifications. Where one sells stock, reserving the dividends, any claim for dividends primarily is against the corporation and not against the purchaser.²

§ 3704. Rights as between pledgor and pledgee. The pledgee of stock has the right to collect dividends on it and apply such dividends to the reduction of the debt.³ However, a pledgee of stock may waive his right to dividends by acquiescing in payment of them to the pledgor.⁴

§ 3705. Rights of legatees and distributees.⁵ A bequest of specific shares of stock does not carry with it stock dividends declared after the execution of the will and before the testator's death.⁶

⁹⁸ Rossi v. Rex Consol. Min. Co., 108 Wash. 296, 183 Pac. 120.

⁹⁹ Segerstrom v. Holland Piano Mfg. Co., 142 Minn. 104, 170 N. W. 930.

¹ Johnson v. Goodenough, 103 Wash. 625, 175 Pac. 306.

² Johnson v. Goodenough, 103 Wash. 625, 175 Pac. 306.

³ Savings Union Bank & Trust Co. v. Crowley, 176 Cal. 553, 169

Pac. 67; Brightson v. Claffin, 225 N. Y. 469, 122 N. E. 458; Western Securities Co. v. Silver King Consol. Min. Co., — Utah —, 192 Pac. 664.

⁴ Welden v. Stephens Farm Loan Co., — Mo. —, 213 S. W. 54.

⁵ See also § 3711 et seq., infra.

⁶ Hicks v. Kerr, 132 Md. 693, 10 A. L. R. 1323, 104 Atl. 426.

§ 3709. Interpleader. Where the company is put on notice of apparently conflicting claims to dividends, it pays a dividend to one not a registered shareholder at its peril.⁷

§ 3710. Assignment or transfer of dividends. Of course the owner of stock may assign the dividends declared thereon.⁸

§ 3711. Right to dividends as between life tenant and remainderman—Dividends declared before creation of the trust.⁹

§ 3712. — Ordinary cash dividends earned after creation of trust. Cash dividends go to the life tenant as "income."¹⁰

§ 3713. — Rule that all cash dividends go to life tenant. This is the rule, it seems, in Rhode Island,¹¹ and West Virginia.¹²

§ 3714. — Rule that all stock dividends are capital. In Maine, a stock dividend goes to the remainderman where there is nothing to show the intent of the testator.¹³ In West Virginia, a stock dividend declared out of a surplus earned since the creation of the trust goes to the remainderman rather than the life tenant, and it is said: "Stock dividends are so exceptional in character and utterly different from cash dividends, interest, rents and other sources of ordinary income, that the creator of a trust fund in shares of corporation stock, with a provision for the payment of the income thereof to a life tenant or tenant for years, cannot be deemed to have intended to in-

⁷ *Fidelity Trust Co. v. Newark Milk & Cream Co.*, 89 N. J. Eq. 229, 108 Atl. 57.

⁸ *Segerstrom v. Holland Piano Mfg. Co.*, 142 Minn. 104, 170 N. W. 930.

⁹ Distribution of proceeds, between life tenant and remainderman, where trust fund consists of corporate stock, see *In re United States Trust Co.*, 190 N. Y. App. Div. 494, 180 N. Y. Supp. 12.

For note on "do stock dividends or dividends in stock of other corporations declared before

testator's death, pass to the legatee of original stock," see *L. R. A.* 1918 B 666.

¹⁰ *Security Trust Co. v. Ram-melsburg*, 82 W. Va. 701, 97 S. E. 122.

¹¹ *Rhode Island Hospital Trust Co. v. Peckham*, — R. I. —, 107 Atl. 209.

¹² *Security Trust Co. v. Ram-melsburg*, 82 W. Va. 701, 97 S. E. 122.

¹³ *Harris v. Moses*, 117 Me. 391, 104 Atl. 703.

clude stock dividends in the income so to be disposed of, in the absence of designation thereof as income.”¹⁴

§ 3715. — What are stock and what are cash dividends. Where a statute made it unlawful for a trust company to hold certain stock of another company, and therefore such stock was distributed among the stockholders of the holding company, the distribution is to be treated as a cash dividend, as between life tenant and remaindermen.¹⁵ A dividend consisting of shares in another corporation, where a profit realized in the usual course of business from a transaction entered into and completed after the death of the testator, is income and payable to the life tenant.¹⁶

§ 3716. — Rule that form of dividend is immaterial.¹⁷ The so-called “Pennsylvania” or “American” rule is adopted in Maryland,¹⁸ and California.¹⁹ In Pennsylvania, in case of ordinary dividends, they usually are not apportionable according to when earned.²⁰

§ 3717. — Apportionment according to time when earned—
General statement. In Ohio, stock dividends declared out of earnings, made prior to the date the interest of the life tenant began, go to the remainderman.²¹

¹⁴ Stock dividends do not pass to the beneficiary of a trust as “income,” although based on net earnings or profits accruing after the creation of the trust. *Security Trust Co. v. Rammelsburg*, 82 W. Va. 701, 97 S. E. 122.

¹⁵ *Smith v. Cotting*, 231 Mass. 42, 120 N. E. 177.

¹⁶ *King v. Mercantile Trust & Deposit Co. of Baltimore City*, 133 Md. 110, 104 Atl. 414.

¹⁷ Article on right of life tenant to extraordinary cash or stock dividends, see 3 St. Louis L. Rev. 149-156.

¹⁸ *Krug v. Mercantile Trust & Deposit Co. of Baltimore City*, 133 Md. 110, 104 Atl. 414.

Dividends of earnings made

after the death of the testator are income and payable to the life tenant, no matter whether the dividend be in cash or scrip or stock. *Krug v. Mercantile Trust & Deposit Co. of Baltimore City*, 133 Md. 110, 104 Atl. 414.

Dividends consisting of shares of stock of another corporation are income and belong to the life tenant. *Krug v. Mercantile Trust & Deposit Co. of Baltimore City*, 133 Md. 110, 104 Atl. 414.

¹⁹ *In re Duffill's Estate*, — Cal. —, 183 Pac. 337.

²⁰ *In re McKeown's Estate*, 263 Pa. 78, 106 Atl. 189.

²¹ *Farmers' Loan & Trust Co. v. Whiton*, 173 N. Y. Supp. 890.

§ 3718. — Ordinary and extraordinary dividends. Where the dividend arises from surplus accumulated before the trust came into existence, such dividend goes to the remainderman instead of the life tenant although originally in the form of a stock dividend which stock was sold by the company and the proceeds distributed among the stockholders.²² Payment of cumulative unpaid dividends out of surplus created before the creation of a trust in stock belongs to the life beneficiary.²³ If an extraordinary corporate dividend reduces the corporate assets below their value at the time the trust began, the principal must first be made good before anything is awarded to income.²⁴

§ 3720. — Dividends declared out of capital. A stock dividend is to be deemed capital rather than income, so as to go not to the life tenant but the remainderman, where the additional stock is to be issued for the purpose of representing the capitalization of the company and not for the purpose of making a division of profits.²⁵ When there has been a division of the corporate property, no matter what form it may take, that part thereof which consists of accumulated profits or earnings belongs to the life tenant and that which is capital to the remainderman.²⁶

§ 3726. — Method of determining whether dividends represent income or capital. Directors cannot determine as to whether a dividend payable partly in cash and partly in stock was capital or income, as between a life estate and remainder.²⁷ Moneys arising from the sale of corporate property and distributed as a cash dividend are income if they arise from a sale of property made by the corporation in the ordinary course of its business, when it sells only such property as its regular

²² Rhode Island Hospital Trust Co. v. Peckham, — R. I. —, 107 Atl. 209.

²³ Thompson v. New York Trust Co., 107 N. Y. Misc. 245, 177 N. Y. Supp. 299.

²⁴ In re McKeown's Estate, 263 Pa. 78, 106 Atl. 189.

²⁵ Palmer v. Pullman Co., 252 Fed. 286.

²⁶ United States Trust Co. v. Heye, 224 N. Y. 242, 120 N. E. 645, aff'g 181 App. Div. 544, 168 N. Y. Supp. 1051.

²⁷ Smith v. Cotting, 231 Mass. 42, 120 N. E. 177.

business is to sell.²⁸ Determination of the directors as to the source of its dividends has no binding or persuasive effect on the court on the issue whether a stock dividend constitutes income going to the life tenant or is principal to be held for the remainderman.²⁹

§ 3727. — Intention of testator or donor. The relative rights of life tenants and remaindermen of stock held in trust are to be settled solely by the terms of the trust; and where it is clear that the creator of the trust intended that all dividends should go to the life tenants, stock dividends go to such life tenants.³⁰

§ 3741. Remedies for unlawful payment of dividends—Liability of directors—At common law. Directors are individually liable for an improper declaration of dividends.³¹ Directors are liable as such for declaring a dividend out of capital in the absence of net earnings where they acted without any report of earnings and any investigation of the company's affairs.³² A suit to recover from directors the amount of dividends illegally paid out by them is not affected by the pendency of an action against the same persons as stockholders to recover the dividends received by them.³³ The actual damage recoverable by a corporation against directors for unlawfully paying dividends is the amount by which its capital is depleted by such payments.³⁴

§ 3742. — — Statutory liability.³⁵ Directors "knowingly" declare and pay a dividend when the corporation is insolvent,

²⁸ *Krug v. Mercantile Trust & Deposit Co. of Baltimore City*, 133 Md. 110, 104 Atl. 414.

²⁹ *In re Duffill's Estate*, — Cal. —, 183 Pac. 337.

³⁰ *In re Thompson's Estate*, 262 Pa. 278, 105 Atl. 273.

³¹ *Pardee v. Harwood Elec. Co.*, 262 Pa. 68, 105 Atl. 48.

³² *Fell v. Pitts*, 263 Pa. 314, 106 Atl. 574.

³³ *Hodde v. Nobbe*, — Mo. App. —, 221 S. W. 130.

³⁴ *Southern California Home Builders v. Young*, — Cal. App. —, 188 Pac. 586.

³⁵ The New York statute, as construed in *De Raimes v. United States Lithograph Co.*, 161 N. Y. App. Div. 781, 146 N. Y. Supp. 813, as set forth in volume 6 of *Fletcher*, p. 6228, note 39, is overruled, although no reference is made thereto, by *German-American Coffee Co. v. Diehl*, 216 N. Y. 57, 109 N. E. 875, which holds

as that word is used in the statute, where they knew the company was not in condition to pay the dividends out of any surplus, or from the circumstances knowledge must be imputed to them.³⁶ The fact that at the time dividends are declared the corporation has outstanding executory contracts carrying a monetary obligation does not make the directors liable for paying unwarranted dividends under the Pennsylvania statute.³⁷ The statutory liability of directors for wrongfully paying dividends is not affected by the fact that after such payment an assessment on stockholders was collected in excess of such payment, where such assessment is not shown to have been levied for the purpose of replacing assets wrongfully diverted.³⁸

A corporation was not "insolvent" when a dividend was declared, so as to make directors personally liable, where it had surplus sufficient to pay its debts and the dividend, and its subsequent insolvency was caused by a decline in the price of raw material bought before the declaration of the dividend.³⁹

Under the Oklahoma statute, making directors liable when they pay dividends except from surplus profits, dissolution of the corporation is a condition precedent whether the recovery is in behalf of the corporation or its creditors.⁴⁰

§ 3743. — Nature and extent of liability. The 1874 Pennsylvania statute making directors individually liable for debts

that the statute does not merely confer a remedy to enforce a statute of the home state of a corporation but instead creates a cause of action to recover the prohibited dividends regardless of whether such dividends could be recovered back in the home state.

³⁶ *Hodde v. Nobbe*, — Mo. App. —, 221 S. W. 130.

³⁷ *United States Smelting Co. v. Hofkin*, 261 Fed. 546, rev'd on other grounds 266 Fed. 679.

³⁸ *Southern California Home Builders v. Young*, — Cal. App. —, 188 Pac. 586.

³⁹ *Hofkin v. United States*

Smelting Co., 266 Fed. 679, rev'g 261 Fed. 546, which held that, under the Pennsylvania statute making directors personally liable for corporate debts where they pay dividends which render the corporation insolvent, they are liable where they declared a 500 per cent dividend after being in business 19 months, although at the time there were ample assets to pay the debts, where subsequent insolvency was due to a large decline in the market price of raw material.

⁴⁰ *Stevirmac Oil & Gas Co. v. Smith*, 259 Fed. 650, so holding where action was by receiver.

where they declare a dividend while the company is insolvent is both penal and remedial.⁴¹ Liability for "debts of the company then existing and for all thereafter contracted" includes purely executory contracts.⁴²

§ 3744. — Effect of good faith. Good faith on the part of directors in declaring dividends from capital instead of from surplus profits is no defense in a suit to hold the directors personally liable, at least where no exceptional circumstances appear.⁴³ However, the liability of a national bank director for declaring dividends out of capital is not absolute, and he is not liable if he acts in good faith.⁴⁴

§ 3746. — By whom liability may be enforced. A corporation may sue directors for wrongfully paying dividends in violation of statute, although suing in its own behalf and not in behalf of creditors.⁴⁵ Where a statute, such as the Illinois one, makes directors who declare a dividend, when the corporation is insolvent, "jointly and severally liable for all the debts of such corporation," the right of action is only in favor of creditors and is personal to them and is not enforceable by the trustee in bankruptcy of the corporation.⁴⁶ Receivers may sue directors to recover dividends unlawfully paid.⁴⁷ Assent of

⁴¹ *United States Smelting Co. v. Hofkin*, 245 Fed. 896, discussing also question as to whether the corporation was insolvent.

⁴² *United States Smelting Co. v. Hofkin*, 245 Fed. 896, 899, construing Pennsylvania statute.

⁴³ *Southern California Home Builders v. Young*, — Cal. App. —, 188 Pac. 586.

Directors who paid dividends from capital are liable, under the statute, although they were led to believe there were surplus profits by the figures of a balance sheet prepared by the corporate employees, and had relied on legal advice and an audit of the books by a public accountant.

Southern California Home Builders v. Young, — Cal. App. —, 188 Pac. 586.

⁴⁴ *Williams v. Spensley*, 251 Fed. 58.

⁴⁵ *Southern California Home Builders v. Young*, — Cal. App. —, 188 Pac. 586.

⁴⁶ *Seegmiller v. Day*, 249 Fed. 177.

⁴⁷ *Hodde v. Nobbe*, — Mo. App. —, 221 S. W. 130.

Officers of a bank who participate in declaring a dividend out of capital of an insolvent company are liable to the receiver for the amount of dividends received by them. *Wood v. Noyes*, 245 Fed. 742.

stockholders to illegal payment of dividends is no defense to an action against directors, brought by a receiver who also represents creditors, to recover the amount paid.⁴⁸ Creditors, by taking charge of a corporation and trying to operate it for their benefit, are not estopped to recover, through a receiver afterwards appointed, unlawful dividends paid by directors, by suing the directors therefor.⁴⁹ Subsequent creditors may, it seems, complain of dividends wrongfully paid and hold the directors liable therefor.⁵⁰

§ 3750. — Criminal liability of directors and officers. In case of building and loan associations, statutes in some states make directors criminally liable for declaring dividends where there are no net earnings.⁵¹

XVII. DIVIDENDS ON PREFERRED STOCK

§ 3751. Right to and extent of preference in general.⁵² Preferred stockholders whose dividends are cumulative and in arrears have no enforceable claim against the corporation until a dividend is declared, and hence are not creditors until such time.⁵³ Where preferred stock is issued at different times, and a dividend is declared on preferred stock from the date the stock was issued, a preferred stockholder is entitled only to a dividend from the time his stock was issued to him and not from the time the preferred stock as a whole was issued.⁵⁴

The "Rights of holders of preferred stock in respect to dividends" is the subject of a lengthy note in a recent volume of the American Law Reports.⁵⁵

§ 3752. Dividends payable out of profits only. The words "surplus net profits," as used in certificates of preferred stock providing that holders are entitled to dividends therefrom, do

⁴⁸ *Hodde v. Nobbe*, — Mo. App. —, 221 S. W. 130.

⁴⁹ *Hodde v. Nobbe*, — Mo. App. —, 221 S. W. 130.

⁵⁰ *Hodde v. Nobbe*, — Mo. App. —, 221 S. W. 130.

⁵¹ *State v. Shuey*, 107 Wash. 437, 181 Pac. 890.

⁵² See also § 3661, *supra*.

⁵³ *Wilder v. Trefry*, — Mass. —, 125 N. E. 689.

⁵⁴ *Waldmann v. Mutual Candy Co.*, 170 N. Y. Supp. 884.

⁵⁵ 6 A. L. R. 802, annotating *Englander v. Osborne*, 261 Pa. 366, 6 A. L. R. 800, 104 Atl. 614.

not mean merely surplus carried on the books but "contemplates surplus net profits over and above all surplus and reserves made by the directors in the exercise of their discretion for the purpose of properly conducting the corporate business."⁵⁶

§ 3753. Discretion in declaring dividends. A preferred stock certificate drawn in the usual terms, with provision as to cumulating dividends, does not make it mandatory on the directors to declare a dividend out of the first profits, although a certificate may be so drawn as to have that effect.⁵⁷ A preferred stock certificate providing that the holders "are entitled out of any and all surplus net profits whenever ascertained to cumulative dividends" at a certain rate in a year beginning on a certain day and in every year thereafter, payable in quarterly instalments "in preference and priority to any payment on any dividend on the common stock for such quarter" does not make the declaration of dividends obligatory.⁵⁸

§ 3754. Cumulative dividends.⁵⁹ Where preferred stock is cumulative, current dividends on such stock should be paid before paying back dividends.⁶⁰ Where there are no accumulated profits, a corporation, on winding up, after paying preferred stockholders the full par value of their stock, should apply the balance, less than the par value of the common stock, to the common stock rather than to the payment of back cumulative dividends on the preferred.⁶¹ It is not an abuse of discretion

⁵⁶ *Hastings v. International Paper Co.*, 187 N. Y. App. Div. 404, 175 N. Y. Supp. 815.

⁵⁷ *Hastings v. International Paper Co.*, 187 N. Y. App. Div. 404, 175 N. Y. Supp. 815.

⁵⁸ *Hastings v. International Paper Co.*, 187 N. Y. App. Div. 404, 175 N. Y. Supp. 815.

⁵⁹ See also § 3661, *supra*.

⁶⁰ *Kennedy v. Carolina Public Service Co.*, 262 Fed. 803.

⁶¹ *Michael v. Cayey-Caguas Tobacco Co.*, 190 N. Y. App. Div. 618, 180 N. Y. Supp. 532 [reviewing *In re Transvaal Co.*, (1896) L. R. 2 Ch. 750; *In re W. J. Hall &*

Co., (1909) L. R. 1 Ch. 521; *In re Espuela Land & C. Co.*, (1909) 2 Ch. 187.]

There are no accumulated dividends payable to preferred stockholders on dissolution of the corporation, in preference to the holders of common stock, where there were no profits since the last dividend on the preferred stock. *Michael v. Cayey-Caguas Tobacco Co.*, 190 N. Y. App. Div. 618, 180 N. Y. Supp. 532, where the certificate of incorporation provided that on dissolution, preferred stockholders should first be paid the par value of their stock

to refuse to declare a 33½ per cent cash dividend on deferred cumulative dividends, although a surplus is available to pay in cash, where the corporation is a paper company enriched by the world war for the first time, and instead to declare a dividend payable 7½ per cent in cash, 14 per cent in cumulative preferred stock, and 12 per cent in common stock.⁶²

§ 3755. Right to share in surplus after payment of preferred dividends. While there is a conflict in the authorities, it is held in Maine that where the contract with preferred stockholders is that they shall receive a certain fixed preferential dividend and in case of liquidation one hundred per cent, such stockholders are entitled to no greater share of the profits than the fixed per cent; and that hence preferred stockholders cannot, against the objection of common stockholders, be given a preemptive right the same as common stockholders to purchase an issue of common stock at a price less than its value, since in effect an additional dividend to the preferred stockholders.⁶³

In Pennsylvania it is held that preferred stockholders are entitled to share with the common stockholders all profits distributed after the latter have received in any one year an amount equal to the dividend on the preferred stock.⁶⁴ Where the six per cent dividends on preferred stock are expressly declared to be cumulative, and no dividends are paid for nine years when a dividend of fifty-four per cent is declared on the preferred stock and a like amount on the common stock, a preferred stockholder can restrain payment of the dividend on the common on the theory that common stock was not entitled to more than six per cent without sharing the excess equally with the preferred stockholders, although the certificates of preferred stock provide for the payment of an annual six per cent dividend "before any dividend shall be set apart on the common stock," since each new year marks the beginning of a new dividend paying period.⁶⁵

and "all accrued and unpaid dividends thereon."

⁶² *Hastings v. International Paper Co.*, 187 N. Y. App. Div. 404, 175 N. Y. Supp. 815.

⁶³ *Stone v. United States Envelope Co.*, — Me. —, 111 Atl. 536.

See also *Will v. United Lankat Plantations Co.*, [1912] L. R. 2 Ch. Div. 571, [1914] A. C. 11.

⁶⁴ *Englander v. Osborne*, 261 Pa. 366, 6 A. L. R. 800, 104 Atl. 614.

⁶⁵ *Englander v. Osborne*, 261

XVIII. THE RIGHT TO TRANSFER SHARES

§ 3758. In general. Stock may be transferred by a client to his attorney to be sold on a commission.⁶⁶ An attorney at law, employed to procure a charter, has no power to consent to a transfer of stock, on behalf of the company.⁶⁷

§ 3759. Restrictions in the charter or general law.⁶⁸ The certificate of incorporation may forbid transfers of stock without first offering it for sale to the other stockholders.⁶⁹ In case of water companies furnishing water only to stockholders, a purchase of stock without the land obtains no title to the stock, under the California statutes.⁷⁰ An offer to sell to a corporation shares of its own stock is not within a charter provision requiring its shareholders to notify the company of any bona fide offer made therefor and giving it the privilege of buying at the same price within a specified time.⁷¹

§ 3761. Agreements in restraint of the right to transfer—In general. A devise of stock may be void as suspending the power of alienation.⁷² Bequests of corporate stock must not violate the statute as to perpetuities by directing an accumulation of income.⁷³

§ 3762. — Agreements giving corporation or other stockholders prior right to purchase. An agreement between all the stockholders that the corporation shall have the exclusive right to purchase their stock for sixty days after notice of a desire to sell is valid and not an unlawful restriction on the power

Pa. 366, 6 A. L. R. 800, 104 Atl. 614.

⁶⁶ *Bailey v. Security Trust Co.*, 179 Cal. 815, 177 Pac. 444.

⁶⁷ *Schmitt v. Kulamer*, — Pa. —, 110 Atl. 169.

⁶⁸ Construction of prohibition against transfer of stock without consent of the directors, where one director refuses to attend meetings, see *In re Copal Varnish Co.*, [1917] 2 Ch. Div. 349.

⁶⁹ *Bloomington v. Bloomington*

dale, 107 N. Y. Misc. 646, 177 N. Y. Supp. 873.

⁷⁰ *Security Commercial & Savings Bank of El Centro v. Imperial Water Co.*, — Cal. —, 192 Pac. 22.

⁷¹ *Durham Life Ins. Co. v. Moize*, 175 N. C. 344, 95 S. E. 552.

⁷² *In re Allen's Will*, 111 N. Y. Misc. 93, 181 N. Y. Supp. 398.

⁷³ *In re Megrue*, 224 N. Y. 284, 120 N. E. 651.

of alienation.⁷⁴ Where one of three stockholders agreed not to transfer his shares to any person until first offering them for sale to another of the three at the same price offered by the third person, failure to exercise the option within a reasonable time bars any right to exercise it.⁷⁵ Where stock is sold a third person in violation of a contract giving the corporation the first right to purchase it, the corporation may sue for specific performance and to cancel the sale, since the remedy at law is inadequate.⁷⁶

§ 3763. Restrictions in stock certificates. A corporation cannot be compelled to transfer stock on its books where the certificate recites that it is transferable "subject to the rules and restrictions provided by the by-laws," and where the stock has not been first offered to the corporation at par as required by such by-laws.⁷⁷

§ 3764. Transfers to or by directors or other officers. Officers of a corporation may join to purchase stock of the corporation from a third person, where they act in good faith.⁷⁸

XIX. EFFECT OF TRANSFER

§ 3768. General principles. A person to whom stock was issued but who had transferred it to one who had full notice of facts affecting its validity is not a necessary party to a suit by the corporation to cancel such stock.⁷⁹

§ 3769. Liability for calls—General rules. A transferee of stock, after the transfer is entered on the corporate books, is liable to the corporation for the balance unpaid on the stock, where no calls therefor have been made before the transfer

⁷⁴ A sale in violation thereof to a business rival with notice may be canceled. *Model Clothing House v. Dickinson*, — Minn. —, 178 N. W. 957.

⁷⁵ *Lockward v. Evans*, 88 N. J. Eq. 530, 102 Atl. 19, aff'd 88 N. J. Eq. 597, 103 Atl. 1053 (mem. dec.).

⁷⁶ *Model Clothing House v.*

Dickinson, — Minn. —, 178 N. W. 957.

⁷⁷ *Chaffee v. Farmers Co-Op. Elevator Co.*, 39 N. D. 585, 168 N. W. 616.

⁷⁸ *Du Pont v. Du Pont*, 256 Fed. 129, aff'g 251 Fed. 937.

⁷⁹ *American Bond & Mortgage Co. v. Lindsay*, — Cal. App. —, 190 Pac. 192.

on the books; but a purchaser of stock is not liable on calls made prior to the transfer of the stock to him on the corporate books.⁸⁰ A statute providing that one becoming a stockholder by transfer of stock shall succeed to all rights and liabilities of prior stockholders does not authorize a transferrer of stock, who has been compelled to pay up his subscription after the transfer, to obtain reimbursement from the transferee.⁸¹

§ 3771. — Stock issued as full paid; watered or fictitiously paid up stock. In construing a North Dakota statute making stockholders liable to creditors "to the amount that is unpaid upon the stock held by him," it is held that liability does not exist on the part of a purchaser from a stockholder unless the seller has not paid the corporation in full and the purchaser has knowledge of such fact.⁸² Purchasers of voting trust certificates, in the open market, as a bonus with the purchase of bonds, are not liable as subscribers for unpaid stock in favor of creditors of the corporation.⁸³

§ 3777. Conflict of laws. The issuance and transfer of capital stock and the rights of the holder thereof is governed by the laws of the state which created the corporation.⁸⁴

§ 3778. Effect of pending judicial proceedings; lis pendens. The rule of lis pendens does not apply to a purchaser of stock pending a suit in equity to recover it as trust property.⁸⁵

XX. NEGOTIABILITY OF STOCK CERTIFICATES AND TITLE OF BONA FIDE TRANSFEREES

§ 3779. General rules. Certificates of stock are not negotiable instruments.⁸⁶ Hence an assignment or transfer is necessarily

⁸⁰ Geary St., P. & O. R. Co. v. Bradbury Estate Co., 179 Cal. 46, 175 Pac. 457. ⁸⁵ Maedermot v. Hayes, — Cal. Minn. 415, 172 N. W. 318.

⁸¹ Jones v. Bowman, 181 Ky. 722, 205 S. W. 923. ⁸⁶ Geary St., P. & O. R. Co. v. Bradbury Estate Co., 179 Cal. 46, 175 Pac. 457; Millard v. Green, — Conn. —, 9 A. L. R. 1610, 110 Atl. 177; Merrill v. Focht, — Wis. —, 179 N. W. 813.

⁸² Lavell v. Bullock, — N. D. —, 174 N. W. 764, and see §§ 3587, 3597, supra.

⁸³ Clark v. Johnson, 245 Fed. 442.

⁸⁴ State ex rel. Bodman v. Pro-

subject to inherent infirmities and to all rights and liabilities attached thereto at the time of the assignment.⁸⁷ A transfer of stock is subject to all existing equities, and where one purchases from negligent directors he has no greater right to share in the fund recovered from other officers for negligence than his transferrers would have had.⁸⁸ A purchaser of stock stands in the shoes of the seller so far as his right to attack prior acts of the corporation or other stockholders is concerned.⁸⁹ The legality of acts at a directors' meeting cannot be attacked by subsequent transferees of stock of directors who had taken an active part in such meeting and had approved and voted for such acts.⁹⁰

§ 3781. Quasi negotiability; estoppel. Stock is quasi negotiable.⁹¹ Certificates of stock are not in form or character negotiable instruments, "yet they approximate to them, and in many respects the same rules apply."⁹²

§ 3783. Bona fide purchasers.⁹³ The rule as to bona fide purchasers applies to sales of corporate stock.⁹⁴ A purchaser of stock with notice of equities therein vested in a third person takes title subject thereto.⁹⁵ A pledgee of shares of stock as security for a pre-existing debt is a transferee for value within the rule as to bona fide purchasers.⁹⁶ An assignment of stock

⁸⁷ *Axford v. Western Syndicate Inv. Co.*, 141 Minn. 412, 168 N. W. 97, 170 N. W. 587.

⁸⁸ *Harris v. Rogers*, 190 N. Y. App. Div. 208, 179 N. Y. Supp. 799.

⁸⁹ *Bernheim v. Wallace*, 186 Ky. 459, 217 S. W. 916.

⁹⁰ *Berman v. Minneapolis Photo Engraving Co.*, 144 Minn. 146, 174 N. W. 735.

⁹¹ *Paine, Webber & Co. v. Arkansas & Arizona Copper Co.*, 136 Ark. 385, 206 S. W. 477.

⁹² *Hudson Trust Co. v. American Linseed Co.*, 190 N. Y. App. Div. 289, 180 N. Y. Supp. 17.

⁹³ See *American Nat. Bank v. Drew*, 175 N. C. 79, 94 S. E. 708.

Recording of deed conveying property of water company as constructive notice of transfer of stock of the company, see *Security Commercial & Savings Bank of El Centro v. Imperial Water Co.*, — Cal. —, 192 Pac. 22.

⁹⁴ *American Trust & Banking Co. v. Union Security Co.*, — Cal. App. —, 184 Pac. 508.

Constructive notice as preventing purchaser of stock being bona fide purchaser without notice, see *Holmes v. Doe Run Lead Co.*, — Mo. App. —, 223 S. W. 772.

⁹⁵ *Kuhn v. Wagner*, — Wis. —, 177 N. W. 896.

⁹⁶ *Smitton v. McCullough*, — Cal. —, 189 Pac. 686.

is not effective as against a subsequent purchaser without notice.⁹⁷ A creditor who purchases stock at a sale under his own judgment, without actual or constructive notice of alleged defects in the title, is a bona fide purchaser for value.⁹⁸ Possessors of certificates of stock are prima facie presumed to be bona fide holders.⁹⁹

The rule that one who actively participates in the perpetration of a fraud cannot become the beneficiary thereof prevents the application of the rule that a purchaser of stock, although with knowledge of defects, takes a complete title where he purchases the stock from a bona fide holder.¹

XXI. MODES OF TRANSFERRING SHARES; REGISTRATION

§ 3784. General principles.² As between the parties, and in the absence of statutory regulation, shares of stock may be assigned in any way other personal property may be assigned.³ They may be transferred by a separate written instrument,⁴ or by a blank indorsement of the certificate;⁵ but a mere book entry is not sufficient as a transfer of stock.⁶ A purchaser of stock indorsed in blank may write in the name of any person as assignee or as attorney in fact.⁷ Even if the legal title does not pass, the equitable title to shares of stock passes by a transfer other than by indorsement of the certificate.⁸ A signature of an assignment of stock is good although above the printed

⁹⁷ *Bates v. Werries*, 198 Mo. App. 209, 199 S. W. 758.

⁹⁸ *American Trust & Banking Co. v. Union Security Co.*, — Cal. App. —, 184 Pac. 508.

⁹⁹ *Feehan v. Kendrick*, 32 Idaho 220, 179 Pac. 507.

¹ *Kay v. Piney Coal & Coke Co.*, — W. Va. —, 99 S. E. 501.

² *Cutting v. Woodward*, 255 Fed. 633.

³ *Young v. New Pedrara Onyx Co.*, — Cal. App. —, 192 Pac. 55.

⁴ *Birmingham Trust & Savings Co. v. Cannon*, — Ala. —, 85 So. 768.

⁵ *Valley View Consol. Gold*

Min. Co. v. Whitehead, — Colo. —, 180 Pac. 737; *Staib v. German Ins. Bank*, 179 Ky. 118, 200 S. W. 322.

Indorsement of stock in blank and transfer to a trust company, pursuant to a contract to sell it, divests title. In *re Gaines*, 180 N. Y. Supp. 191.

⁶ *State ex rel. Smit v. Lafayette Bldg. Ass'n*, 147 La. 526, 85 So. 228.

⁷ *Valley View Consol. Gold Min. Co. v. Whitehead*, — Colo. —, 180 Pac. 737.

⁸ *Young v. New Pedrara Onyx Co.*, — Cal. App. —, 192 Pac. 55.

assignment.⁹ Possession of a certificate of stock, while not of itself evidence of ownership, is such evidence where coupled with a written assignment of the holder, except where the relations between the ex-owner and the possessor are intimate and the latter had access to the former's property, as in case of an executor or trustee.¹⁰

§ 3785. Necessity for delivery.¹¹ Delivery of stock is not necessary to pass title.¹² However, there is no sale of stock, as against an attaching creditor, where a bill of sale is executed but the certificate is not delivered because lost, and a new certificate had not been obtained because of failure to furnish a satisfactory indemnity bond.¹³ Delivery of certificates of stock to a third person to be delivered to another at the death of the depositor vests a present title in the donee, subject to a life estate in the depositor, and is irrevocable.¹⁴

There is no presumption of a delivery of stock on the date of its assignment, in the absence of any proof of delivery.¹⁵

§ 3786. Delivery of certificate without indorsement or assignment. Title to stock may pass although the assignment was not written on the back of the certificate.¹⁶ A delivery of stock without a formal transfer effects an equitable pledge.¹⁷

§ 3788. Necessity for complying with statutory provisions; waiver. The California statute providing how shares of stock "may" be transferred is not exclusive so as to require a transfer by indorsement.¹⁸

⁹ *Fink v. Schleuter*, 206 Ill. App. 159.

¹⁰ *Gaines v. Huyler*, 184 N. Y. Supp. 145.

¹¹ Delivery in escrow, see § 3857, *infra*.

Delivery to complete gift, see § 3947, *infra*.

¹² *Young v. New Pedrara Onyx Co.*, — Cal. App. —, 192 Pac. 55; *Allen v. Williams*, 212 Ill. App. 114.

¹³ *Lucifer Coal Co. v. Buster*, 64 Colo. 179, 171 Pac. 61.

¹⁴ *Coward v. De Cray*, 38 Cal. App. 290, 176 Pac. 56.

¹⁵ *Gaines v. Huyler*, 184 N. Y. Supp. 145.

¹⁶ *Mitchell v. Beachy*, 104 Kan. 445, 179 Pac. 365.

¹⁷ *Millard v. Green*, — Conn. —, 9 A. L. R. 1610, 110 Atl. 177.

¹⁸ *Young v. New Pedrara Onyx Co.*, — Cal. App. —, 192 Pac. 55.

§ 3792. Mode of procuring transfer on books, and sufficiency of transfer—Upon whom demand for registration should be made. A demand on a corporation to transfer stock is properly made on the secretary.¹⁹ Ordinarily a demand to transfer bank stock on the books is properly made on the cashier.²⁰

§ 3793. Issue of certificate to transferee, and surrender of old certificate.²¹ The owner of stock represented by a single certificate has the right to surrender such certificate and have new certificates made out for a smaller number of shares in the names of anyone whom he sees fit.²²

XXII. EFFECT OF UNREGISTERED TRANSFERS

§ 3794. Effect of unregistered transfers as between the parties. A transfer of stock is valid, as between the parties, although not registered on the corporate books as required by statute.²³

§ 3798. Effect of unregistered transfers as against the corporation—General rule. While ordinarily notice of the assignment of shares of stock must be given to the corporation, notice is not necessary where there is involved merely the rights as between themselves of two assignees of equitable interests.²⁴

§ 3799. — Right to vote.²⁵

§ 3801. — Liability for calls or assessments. A buyer of stock is liable for a balance due on the subscription, although he had a right to have the sale set aside, where he has elected not to rescind, although no transfer has been made on the books.²⁶

¹⁹ Hight v. Farmers' Grain Co., 214 Ill. App. 195.

²⁰ Bank of Norwood v. Ray, 21 Ga. App. 620, 94 S. E. 819.

²¹ See also § 3816 et seq., *infra*.

²² Wallace v. Citizens' State Bank, 205 Ill. App. 7.

²³ Birmingham Trust & Savings Co. v. Cannon, — Ala. —, 85 So. 768; D. I. Felsenthal Co. v. North-

ern Assur. Co., Ltd., of London, 205 Ill. App. 610, *aff'd* 284 Ill. 343, 120 N. E. 268; Fidelity Trust Co. v. Newark Milk & Cream Co., — N. J. L. —, 108 Atl. 54.

²⁴ Smitton v. McCullough, — Cal. —, 189 Pac. 686.

²⁵ See § 1663, *supra*.

²⁶ Wichita Union Terminal R. Co. v. Kansas City, M. & O. R.

§ 3802. — Payment of dividends.²⁷

§ 3809. — Refusal to register transfer. Where a stockholder has done all in his power to secure the registry of stock, his rights are the same as if the registry had been made.²⁸

§ 3810. Effect of unregistered transfer as against corporate creditors. A transferee of stock, where not registered, is not liable to creditors for unpaid subscriptions on the stock.²⁹

§ 3811. Effect of unregistered transfer as against creditors of apparent owner—General rules. After stock is transferred, it cannot be levied on as the property of the transferee even though the transfer is not made on the corporate books.³⁰ In California, an execution purchaser of stock registered in the name of the judgment debtor, is entitled thereto as against an unregistered transfer of which he had no notice.³¹ In Colorado, the rule that an unregistered transfer of stock is invalid as against creditors applies only to lien creditors.³² Under the Colorado statutes requiring transfers of stock to be entered on the corporate books, execution cannot be levied on the right of a holder of a stock certificate not transferred on the corporate books to him.³³

§ 3815. Effect of unregistered transfers as against purchasers or pledgees from apparent owners. If a pledge of stock is not noted on the books of the corporation, a bona fide purchaser at an execution sale of such stock standing on the books

Co., 100 Kan. 83, 163 Pac. 1067, and see § 3769 et seq., supra.

²⁷ See §§ 3700-3703, supra.

²⁸ Carlton v. Camfield, 64 Colo. 373, 171 Pac. 1140, and see § 3816 et seq., infra.

²⁹ Marks v. Brenner, 204 Ill. App. 366.

³⁰ Allen v. Williams, 212 Ill. App. 114.

³¹ Security Commercial & Savings Bank of El Centro v. Imperial Water Co., — Cal. —, 192 Pac. 22.

³² Carlton v. Camfield, 64 Colo. 373, 171 Pac. 1140.

An unregistered transfer of shares is valid as against creditors of an insolvent estate whose claims have been allowed before an attempt was made to register the transfer. Carlton v. Camfield, 64 Colo. 373, 171 Pac. 1140.

³³ Snider v. Bourquin, — Colo. —, 188 Pac. 727.

in the name of the pledgor is protected in his purchase as against the pledgee.³⁴ A pledgee of stock need not have the pledge transferred on the books except as against subsequent purchasers in good faith for value and without notice of the equities.³⁵

XXIII. REFUSAL TO RECOGNIZE AND REGISTER TRANSFERS

§ 3816. Right to transfer and duty to make it. The owner of stock may compel corporate officers to transfer the stock on the corporate books to his name.³⁶ So the court may compel a transfer of stock on the corporate books at the instance of an equitable owner who seeks by the transfer to consummate a legal title.³⁷ In an action by an assignee of stock to compel the corporation to deliver the certificate and register the assignment on the books, claims against the assignor cannot be set off.³⁸

§ 3817. Remedies for refusal to transfer—Suit in equity to compel transfer.³⁹ Equity has jurisdiction of an action by a transferee of stock against the corporation to compel it to transfer the stock and issue a new certificate.⁴⁰ Mandamus to compel a transfer of stock on the books is not such an adequate remedy as to oust a court of equity from jurisdiction.⁴¹ One who does not come with clean hands is not entitled to the aid of equity to compel registration of his certificate of stock.⁴²

All owners of stock represented by a single certificate may

³⁴ American Trust & Banking Co. v. Union Security Co., — Cal. App. —, 184 Pac. 508.

³⁵ Seymour v. Salsberry, — Cal. —, 171 Pac. 938.

³⁶ Orvis v. Howe, 183 N. Y. App. Div. 1, 170 N. Y. Supp. 264; Lorsch & Co. v. Shamrock Consol. Mines, Ltd., 36 Dom. L. Rep. (Can.) 557.

³⁷ Lockward v. Evans, 88 N. J. Eq. 530, 102 Atl. 19, aff'd 88 N. J. Eq. 597, 103 Atl. 1053 (mem. dec.).

³⁸ Lask v. Bedell (N. J. Ch.), 109 Atl. 849.

³⁹ See also § 3484, supra.

⁴⁰ Oden v. Vaughn, — Ala. —, 85 So. 779; Massengale v. Hodgson, 148 Ga. 97, 95 S. E. 975; Lask v. Bedell (N. J. Ch.), 109 Atl. 849.

Equity will compel a transfer of stock on the books without regard to whether title was acquired through a mortgage or a pledge. Oden v. Vaughn, — Ala. —, 85 So. 779.

⁴¹ Oden v. Vaughn, — Ala. —, 85 So. 779.

⁴² Mitchell v. Leland Co., 246 Fed. 103.

join in a suit to compel a proper transfer of such shares on the books.⁴³ In a suit to compel a transfer on the books, a corporate officer alleged to have unreasonably refused to make the transfer, is a necessary defendant where he is sought to be held personally.⁴⁴ In a suit to set aside a rescission of an exchange of stock and to require proper registration on the books, one claiming title as pledgee is a necessary defendant.⁴⁵

§ 3818. — Mandamus to compel transfer. Mandamus lies to compel a transfer of stock on the books, where a corporate duty, in Louisiana⁴⁶ and West Virginia.⁴⁷ So in Colorado mandamus lies to compel a corporation to issue stock to a person entitled thereto.⁴⁸ In mandamus to compel a transfer of stock on the books, claimants of the stock should be joined as parties,⁴⁹ and where the pledgee sues, the pledgor is a necessary party.⁵⁰

§ 3819. — Action against corporation for damages. Refusal to transfer stock on the books, where wrongful, is a conversion,⁵¹ and makes the corporation liable for any damages resulting therefrom.⁵²

Refusal to transfer shares on the books calls for at least nominal damages.⁵³ The measure of damages for refusing to transfer stock on the books is the value of the stock at the time of the demand and refusal.⁵⁴

§ 3822. — Statutory remedies. An action against a corporate secretary for the statutory penalty for refusal to transfer

⁴³ Wallace v. Citizens' State Bank, 205 Ill. App. 7.

⁴⁴ Orvis v. Lorraine, 183 N. Y. App. Div. 1, 170 N. Y. Supp. 264.

⁴⁵ Young v. New Pedrara Onyx Co., — Cal. App. —, 192 Pac. 55.

⁴⁶ State ex rel. Smit, v. Lafayette Bldg. Ass'n, 147 La. 526, 85 So. 228.

⁴⁷ Citizens' Nat. Bank of Port Allegheny v. Consolidated Glass Co., 83 W. Va. 1, 97 S. E. 689.

⁴⁸ Capital Petroleum Co. v. Holdeman, — Colo. —, 180 Pac. 758.

⁴⁹ People ex rel. Staver v. Elgin

Motor Car Corporation, 209 Ill. App. 601.

⁵⁰ Lask v. Bedell (N. J. Ch.), 109 Atl. 849.

⁵¹ See Gorham v. Massillon Iron & Steel Co., 284 Ill. 594, 120 N. E. 467.

⁵² Citizens' Bank v. Bank of Penfield, — Ga. App. —, 101 S. E. 203; Bank of Norwood v. Ray, 21 Ga. App. 620, 94 S. E. 819.

⁵³ Kingsbury v. Riverton-Wyoming Refining Co., — Colo. —, 192 Pac. 503.

⁵⁴ Bank of Norwood v. Ray, 21 Ga. App. 620, 94 S. E. 819.

stock may be brought immediately after the refusal on an untenable ground.⁵⁵

§ 3823. Refusal must be wrongful—In general.⁵⁶ If a corporation is under no duty to transfer on its book stock sold under attachment, then of course its refusal to transfer such stock is not a conversion.⁵⁷ A transfer on the books is properly refused where the stock is in custody of the law by virtue of an attachment.⁵⁸ Transfer of shares cannot be refused because the transferrer is indebted to the company, where it has no lien on the stock.⁵⁹

Power conferred on directors to refuse to register transfers of stock if "in their opinion it is contrary to the interests of the company that the proposed transferee should be a member thereof" justifies a refusal to transfer only on grounds personal to the proposed transferee, and not on the ground that it is undesirable to increase the number of stockholders.⁶⁰

§ 3824. — Effect of conflicting claims to same stock. Corporate officers are justified in refusing to transfer stock on the books where the assignor in whose name the stock stands sets up a conflicting claim thereto because of defects as to the consideration for the assignment.⁶¹

§ 3828. — Right to require proof of authority—Where stock is held in a fiduciary capacity. The fact that the will of a nonresident stockholder has not been admitted to probate in the domicile of the corporation, and the absence of creditors with claims on the stock determined, is no reason for refusing to transfer the stock on the books, the transfer having been made by the executors.⁶²

⁵⁵ *Bowring v. Prime*, — Cal. App. —, 189 Pac. 701.

⁵⁶ Necessity for stamps, see § 4627a, *infra*.

⁵⁷ *Harris v. Mid-Continent Life Ins. Co.*, — Okla. —, 182 Pac. 85.

⁵⁸ *Gorham v. Massillon Iron & Steel Co.*, 209 Ill. App. 606, *aff'd* 284 Ill. 594, 120 N. E. 467.

⁵⁹ *Kingsbury v. Riverton-Wy-*

oming Refining Co., — Colo. —, 192 Pac. 503.

⁶⁰ *In re Bede Steam Shipping Co., Ltd.*, [1917] 1 Ch. Div. 123.

⁶¹ *People ex rel. Staver v. Elgin Motor Car Corp.*, 209 Ill. App. 601.

⁶² *Way v. International Portland Cement Co.*, 100 Wash. 182, 170 Pac. 553.

XXIV. FORGED AND UNAUTHORIZED TRANSFERS, AND TRANSFERS IN
BREACH OF TRUST

§ 3830. Duty of corporation with respect to transfers. A corporation is under no duty to determine the title to stock presented for transfer, as to whether the agent presenting the stock for transfer violated his instructions, where the stock is indorsed in blank.⁶³ An action against a corporation to obtain a transfer of stock and the dividends declared on said shares, on the theory that a transfer of such stock on the books to another under a blank indorsement was in violation of plaintiff's instructions, is barred by failure to sue for over two years during which time the stock became valuable.⁶⁴ A subsequent holder of stock is not charged with any duty to discover if the signature of the registrar is genuine.⁶⁵

§ 3832. Failure to require surrender of original certificate. Negligence of the corporation in failing to cancel a certificate of stock delivered to the corporation for cancellation and reissuance, resulting in embezzlement of the stock by an employee, makes the corporation liable for resulting damages.⁶⁶

§ 3835. Transfers by persons under legal disability. The Uniform Transfer Act applies to trustees, executors, etc., where the validity of the transfer is not dependent on the indorsement or assignment of such trustees, executors, etc.⁶⁷ The words "indorsement" and "assignment" as used in the Uniform Transfer Act in regard to the power of infants, trustees, etc., to make a valid "indorsement, assignment" or power of attorney, refer to a writing passing or attempting to pass title to stock.⁶⁸

§ 3836. Unauthorized or fraudulent transfers by agents. A corporation is not liable to a stockholder for transferring his

⁶³ Valley View Consol. Gold Min. Co. v. Whitehead, — Colo. —, 180 Pac. 737.

⁶⁴ Valley View Consol. Gold Min. Co. v. Whitehead, — Colo. —, 180 Pac. 737.

⁶⁵ Hudson Trust Co. v. American Linseed Co., 190 N. Y. App. Div. 289, 180 N. Y. Supp. 17.

⁶⁶ See Paine, Webber & Co. v. Arkansas & Arizona Copper Co., 136 Ark. 385, 206 S. W. 447.

⁶⁷ Stoltz v. Carroll, 99 Ohio St. 289, 124 N. E. 226.

⁶⁸ Stoltz v. Carroll, 99 Ohio St. 289, 124 N. E. 226.

stock on its books pursuant to a blank indorsement although the person presenting the certificate for transfer acted in violation of the owner's instructions to him.⁶⁹ No title to stock is acquired by one through delivery by another who was not the owner nor authorized by the owner to convey or deliver the stock, and where the stock was not indorsed and had been obtained by the person delivering it without knowledge of the owner.⁷⁰ Where the proper corporate officers sign certificates of stock in blank, in quantities, and leave them in an open vault after delivery to a clerk, and such officers exercised no supervision over the issuance of the stock, the corporation is guilty of such negligence as to make it liable to one making a loan on a certificate of stock fraudulently issued by the clerk.⁷¹

§ 3839. Unauthorized or fraudulent transfers by trustees—Use of word "trustee" as notice. Addition of word "trustee" to the name of the registered owner of stock, on the corporate books, does not necessarily show that his title was limited.⁷²

§ 3841. Unauthorized or fraudulent transfers by executors or administrators—Liability of corporation.⁷³

§ 3843. Remedies of owner against corporation. Laches bars a suit by a stockholder against a corporation for wrongfully transferring stock on the books and paying dividends to the transferee.⁷⁴

§ 3846. Liability of transferee to corporation. Where a purchaser of stock presents to the corporation a transfer of shares

⁶⁹ Valley View Consol. Gold Min. Co. v. Whitehead, — Colo. —, 180 Pac. 737.

⁷⁰ Crichton v. Louisiana Oil Refining Co., 144 La. 649, 81 So. 213.

⁷¹ Hudson Trust Co. v. American Linseed Co., 190 N. Y. App. Div. 289, 180 N. Y. Supp. 17, distinguishing Knox v. Eden Musee Co., 148 N. Y. 441, 454, 31 L. R. A. 779, 51 Am. St. Rep. 700, 42 N. E. 988.

⁷² Young v. New Pedrara Onyx Co., — Cal. App. —, 192 Pac. 55.

⁷³ See § 3828, supra.

⁷⁴ Laches bars an action by a stockholder against his corporation for transferring his stock on the books under a blank indorsement but contrary to instructions given the person presenting the certificates for transfer. Valley View Consol. Gold Min. Co. v. Whitehead, — Colo. —, 180 Pac. 737.

accompanied by the certificate, and demands a new certificate in exchange, he impliedly represents that the transfer is valid; and even if a forged transfer is presented by the purchaser in good faith, the corporation which issues new certificates on the faith of them has a right of action on an implied warranty.⁷⁵ A corporation may sue one who presented a forged power of attorney to transfer stock on the faith of which the corporation issues a new certificate of stock, although such person acted in good faith and although the forger guaranteed, as a member of the stock exchange, the genuineness of the signature.⁷⁶ Where there is a guaranty of the signature of a power of attorney to transfer stock, limitations begin to run against the guarantor, in case of forgery, at once.⁷⁷

§ 3849. Liability of person selling stock as broker or agent.

As between a corporation who put it in the power of its clerk to embezzle stock, indorsed in blank and sent to it for cancellation and reissuance, and a broker to whom the clerk sent the stock for sale as his own, the broker must stand the loss where he was negligent in not making inquiries which would have shown that the stock was embezzled.⁷⁸

§ 3853. Estoppel of true owner to assert title as against transferee. Estoppel of the true owner to attack the validity of a transfer of stock arises by clothing another with apparent ownership.⁷⁹ A purchaser of stock from one having apparent title

⁷⁵ *Boston Towboat Co. v. Medford Nat. Bank*, 232 Mass. 38, 121 N. E. 491, holding also there was no contract of indemnification and that limitations began to run at the time of the breach of warranty.

⁷⁶ *Lake Superior Corporation v. Rebre*, 65 Pa. Super. Ct. 379.

⁷⁷ *Boston Towboat Co. v. Medford Nat. Bank*, 232 Mass. 38, 121 N. E. 491, following *Lehigh Coal & Navigation Co. v. Blakeslee*, 189 Pa. 13, 69 Am. St. Rep. 788, 41 Atl. 992.

⁷⁸ *Paine, Webber & Co. v.*

Arkansas & Arizona Copper Co., 136 Ark. 385, 206 S. W. 477.

⁷⁹ *Spellacy v. Young*, — Cal. App. —, 186 Pac. 368; *Crosby v. Simpson*, — Mass. —, 125 N. E. 616; *Bollstrom v. Duplex Power Car Co.*, 208 Mich. 15, 175 N. W. 492.

Of course if the owner of stock permits another to represent himself to be the owner and to sell it, the owner is estopped to attack the validity of the transfer. *Bollstrom v. Duplex Power Car Co.*, 208 Mich. 15, 175 N. W. 492.

is a bona fide purchaser.⁸⁰ To illustrate: a stockholder who indorses his certificate in blank and sends it to a broker for sale cannot complain of acts of a bank relying on the apparent ownership of the broker.⁸¹ So where a corporation, by negligence, allows a certificate of stock to fall into the hands of one with apparent title, and he uses it as collateral for a loan, the rights of the pledgee are superior to those of the corporation.⁸²

XXV. CONTRACTS FOR THE SALE OF SHARES

§ 3857. Formation and validity of contract in general.⁸³ The acceptance of an offer to sell stock is not binding on the seller where not identical with the offer.⁸⁴ A counter proposition to an offer to buy stock is not an acceptance, i. e., an acceptance of the offer to buy so far as part of the number of shares was concerned.⁸⁵ An offer to sell stock may be withdrawn at any time before acceptance.⁸⁶ An executor may contract to sell stock of a corporation.⁸⁷

An option to purchase stock is clearly distinguishable from a contract for the purchase of stock.⁸⁸ It is clearly distinguishable from a contract to sell stock to be deposited in escrow until final payment and which provides for the return of the stock on default in future payments.⁸⁹

The rule against perpetuities should not be extended to an option as to stock of a private corporation.⁹⁰

Stock may be made the subject of an escrow agreement.⁹¹

⁸⁰ Halpern v. Cure, 173 N. Y. Supp. 385.

⁸¹ Snowden v. Marine Nat. Bank, 256 Fed. 350.

⁸² American Nat. Bank v. Dew, 175 N. C. 79, 94 S. E. 708.

⁸³ Sufficiency of evidence to establish contract to transfer a share of stock, see Fidelity Trust Co. v. Newark Milk & Cream Co., — N. J. L. —, 108 Atl. 54.

Rights of assignee of contract to purchase stock, see George v. Ford, 183 Ky. 808, 211 S. W. 438.

Contract for sale of stock held not unilateral, see Mutual Oil Co. v. Hills, 248 Fed. 257.

⁸⁴ Neer v. Lang, 252 Fed. 575,

citing Cameron v. Wright, 21 N. Y. App. Div. 395, 47 N. Y. Supp. 571.

⁸⁵ Butler v. Foley, 211 Mich. 668, 179 N. W. 34.

⁸⁶ Durham Life Ins. Co. v. Moize, 175 N. C. 344, 95 S. E. 552.

⁸⁷ In re Heinze's Estate, 224 N. Y. 1, 120 N. E. 63.

⁸⁸ Heller v. Pope, 183 N. Y. App. Div. 864, 171 N. Y. Supp. 619.

⁸⁹ Western U. Tel. Co. v. Brown, 253 U. S. 101, 64 L. Ed. 803, rev'g Western U. Tel. Co. v. Lange, 248 Fed. 656.

⁹⁰ Kingston v. Home Life Ins. Co., — Del. —, 101 Atl. 898.

⁹¹ Delivery of stock as constituting escrow, see Bailey v. Secu-

§ 3858. Consideration and mutuality. An option to purchase stock is not binding where there is no consideration therefor.⁹² However, an option to purchase stock is based on a sufficient consideration where the person to whom given was thereby induced to surrender a valuable law practice and assume the management of the corporation.⁹³

Mere inadequacy of consideration is not ground for a rescission by a buyer of stock.⁹⁴ Where the purchaser of stock had been vice president for over a month, with every opportunity to learn the condition of the corporation, he cannot defend an action on a note given for the stock on the ground that the stock was worth only a nominal amount.⁹⁵

§ 3859. Oral contracts; statute of frauds—Necessity for writing. Whether a contract to sell stock must be in writing depends on the law of the state where the contract was entered into and the parties resided.⁹⁶ The statute of frauds in many states applies to the sale of stock.⁹⁷ A certificate of stock is "goods, wares or merchandise," within the statute of frauds, in many jurisdictions;⁹⁸ but shares of stock are not real estate within the statute of frauds provision relating to real property.⁹⁹

That the custom is to sell stock over the telephone does not change the rule that contracts for sale of stock must be in writing to satisfy the statute of frauds.¹

§ 3861. Illegality; gambling contracts. The statute relating to margin contracts without intention to make an actual delivery

rity Trust Co., 179 Cal. 815, 177 Pac. 444.

Duty of bank holding stock in escrow, see *Western U. Tel. Co. v. Lange*, 248 Fed. 656.

⁹² *Thomas v. Birch*, 178 Cal. 483, 173 Pac. 1102.

⁹³ *Gorham v. Jackson*, 177 N. Y. Supp. 80.

⁹⁴ *Hallidie v. First Federal Trust Co.*, — Cal. —, 171 Pac. 431; *Hancock v. Luke*, — Utah —, 173 Pac. 137.

⁹⁵ *American Sav. Bank & Trust Co. v. Peterson*, — Wash. —, 191 Pac. 837.

⁹⁶ *Matson v. Bauman*, 139 Minn. 296, 166 N. W. 343.

⁹⁷ *Houston v. Mahoney*, — Mo. App. —, 219 S. W. 128; *Mahoney v. Kennedy*, — Wis. —, 179 N. W. 754. See also *Benner v. Billings*, 107 Wash. 1, 181 Pac. 19.

⁹⁸ *Houston v. Mahoney*, — Mo. App. —, 219 S. W. 128; *Coleman v. St. Paul & T. Lumber Co.*, — Wash. —, 188 Pac. 532.

⁹⁹ *McCullough v. Clark*, 81 W. Va. 743, 95 S. E. 787.

¹ *Houston v. Mahoney*, — Mo. App. —, 219 S. W. 128.

does not apply to a customer as to whom actual deliveries were made, regardless of the relations of the brokers to other customers.² A customer cannot recover from a stockbroker, under the Massachusetts gaming statute, where actual delivery of the stock was contemplated on payment in full.³

A sale of stock in violation of the Blue Sky Law is absolutely void, at least in Michigan, although the statute does not expressly declare such sales to be void.⁴ If a transfer of stock is void because of noncompliance of the corporation with the Blue Sky Law, the rights of the transferrer and transferee are governed, of course, by the rules governing all void transfers of stock.⁵

§ 3863. Effect of fraud and false representations—What amounts to fraud in general.⁶ Any false representation of a material past or existing fact by either party to a contract for the sale of stock constitutes fraud if made with knowledge of its falsity or recklessly, with intent that it be acted on, where relied on by the other party to his injury.⁷ A promise by one selling stock to repurchase it in a year, where made with no intention of fulfillment, is a fraud authorizing a rescission of the contract.⁸ A false statement as to the ownership of stock sold is not necessarily a fraud in law,⁹ nor is inadequacy of consideration, where not gross.¹⁰ A sale of stock to the brother of the majority stockholder was not a fraud as against the seller because of the declaration of large dividends soon thereafter, where such dividends were earned after the execution of the contract.¹¹ That the secretary of the corporation received more

² Barrell v. Paine, — Mass. —, 128 N. E. 17.

³ Bendslev v. Lovell, — Mass. —, 126 N. E. 389.

⁴ See § 4421, *infra*.

⁵ Edward v. Ioor, 205 Mich. 617, 172 N. W. 620.

⁶ Blue Sky Law, see § 4421, *infra*.

⁷ Lentz v. Landers, — Ariz. —, 185 Pac. 821, citing Fletcher Cyc. Corp. § 3863.

Acts as fraudulent in particular cases, see Armstrong v. Rachow, 205 Mich. 168, 171 N. W. 389; Righter v. Parry, 266 Pa.

373, 109 Atl. 917; Harris v. Saunders, 108 Wash. 195, 182 Pac. 949.

Fraud in sale of stock by banker to aged and illiterate farmer woman, what constitutes, see Rowe v. Phillips, 214 Ill. App. 582.

⁸ Lentz v. Landers, — Ariz. —, 185 Pac. 821.

⁹ Reid v. Hughlett, 135 Md. 181, 108 Atl. 477.

¹⁰ Peavey v. Wells, 139 Minn. 174, 165 N. W. 1063.

¹¹ Hutchinson v. Sperry, 261 Fed. 133.

for his stock pooled with others for sale, than the others, does not make him liable to the others where he was under no duty to disclose the price he was to receive and where he in no way influenced the others.¹²

§ 3864. — Representations as to corporate property and assets. A false representation that the company had a patent to the fan proposed to be manufactured is a representation as to a material existing fact and not as to a matter of opinion merely.¹³ Statements of sellers of stock that the corporation owned a patent which had been established in an infringement suit, where false, are ground for rescinding the purchase of stock.¹⁴

§ 3865. — Representations as to financial condition of the corporation. It is fraud to say that the corporation is doing a good business where it is doing business at a loss.¹⁵ A person buying bank stock has no greater right to rely on the accuracy of the books and reports of the bank than he would have to rely on those of any other corporation whose stock he was buying.¹⁶

§ 3867. — Representations as to capital stock. A representation that all the new stock had been subscribed for may be a material one.¹⁷

§ 3868. — Representations as to value of stock. Representations as to the value of the stock sold may constitute actionable fraud.¹⁸ Thus, a representation that stock exchanged for land was worth seventy-five cents on the dollar has been held a representation of fact rather than an opinion.¹⁹ So representations as to the price the stock was selling for at a certain place and as to its value, where false, are actionable as statements of facts rather than expressions of opinion.²⁰ Likewise, where the party

¹² *McCord v. Martin*, — Cal. App. —, 191 Pac. 89.

¹³ *Lentz v. Landers*, — Ariz. —, 185 Pac. 821.

¹⁴ *Kahn v. Revett*, 39 Cal. App. 312, 178 Pac. 733.

¹⁵ *Sherman v. Smith*, 185 Iowa 654, 169 N. W. 216.

¹⁶ *Costello v. Sykes*, 143 Minn. 109, 5 A. L. R. 250, 172 N. W. 907.

¹⁷ *Loomis v. Pease*, — Mass. —, 125 N. E. 177.

¹⁸ *Dalton v. Hopper*, — Okla. —, 177 Pac. 571. See *Zeglin v. Tetzlaff*, — Minn. —, 178 N. W. 954.

¹⁹ *McDonald v. Lastinger*, — Tex. Civ. App. —, 214 S. W. 829.

²⁰ *Farrell v. Hunt*, — Ind. —, 124 N. E. 745.

making false representations as to the value of the stock was president of the corporation, and knew the stock was worthless and that the prospective buyer was relying on his statements as to value, the representation is a statement of an existing fact and not a mere expression of an opinion.²¹

Where a director, in trying to purchase stock from a stockholder, stated his offer was the value of the stock, when he knew the stock was worth double such offer because of a pending deal, the stockholder who sold his stock to such director may recover the difference between the sum he received and the real value.²²

§ 3869. — Further illustrations. Representations to a stockholder that certain stock had been turned back by a subscriber unable to pay for it, and asking him to buy it to help out the company, relate to material matters so as to be ground for rescission.²³ Stockholders who falsely represent to others that if they would pool their stock they could sell it all for five dollars a share, when in fact it was to be sold for eight, are liable to the latter for the difference.²⁴

§ 3870. — Expressions of opinion, promises or predictions. Actionable fraud cannot be predicated on mere promises as to the future²⁵ or matters of opinion.²⁶

§ 3872. — Nondisclosure or concealment of facts. Failure to disclose facts may constitute fraud.²⁷

§ 3874. — Knowledge of falsity and intent to deceive. Knowledge of the maker of the falsity of the representation is immaterial,²⁸ and in some states misrepresentations are actionable although made in good faith.²⁹

²¹ *Lentz v. Landers*, — Ariz. —, 185 Pac. 821, citing *Fletcher Cyc. Corp.* § 3868.

²² *Bollstrom v. Duplex Power Car Co.*, — Mich. —, 175 N. W. 492, and see § 2564, *supra*.

²³ *Stillwell v. Rankin*, 55 Mont. 130, 174 Pac. 186.

²⁴ *McCord v. Martin*, — Cal. App. —, 191 Pac. 89.

²⁵ *Beeman v. Richardson*, —

Cal. App. —, 189 Pac. 790.

²⁶ *Sherman v. Smith*, 185 Iowa 654, 169 N. W. 216. What are mere opinions, see preceding sections.

²⁷ *Sherman v. Smith*, 185 Iowa 654, 169 N. W. 216.

²⁸ *McDonald v. Lastinger*, — Tex. Civ. App. —, 214 S. W. 829.

²⁹ *Loomis v. Pease*, — Mass. —, 125 N. E. 177.

§ 3875. — The representation as an inducement. Fraudulent representations, to be actionable, must have been relied on.³⁰ Knowledge of the buyer that a representation is untrue prevents a recovery for fraud.³¹ False representations not relied on are not ground for annulling a contract to exchange stock for land.³² Material misrepresentations of the value of corporate assets, inducing a purchase of stock, are ground for rescission, but not where the buyer had sufficient notice to put him upon inquiry.³³ That plaintiff is a bookkeeper of a company does not, of course, preclude his right to sue for damages for deceit in sale of stock to him, as to the financial condition of the company.³⁴

Where one who was the vice president and a director of a company sold his stock to the president, the former is not chargeable with notice of the falsity of a financial statement of the affairs of the corporation, prepared by the president.³⁵

§ 3876. — Right to rely on representations. It is held that it is no defense to a fraudulent representation that the other party had an opportunity to ascertain whether the representation was true; ³⁶ but it is also held that there is no fraud of the buyer in inducing a sale of stock where the seller had notice of the conditions and had the opportunity to discover the real facts.³⁷ A purchaser of stock has the right to rely on a representation that the reason the stock was sold much lower than the market was in order to make future business friends.³⁸ False representations as to the financial condition of the company make the seller liable although the corporate books are open to inspection, where they do not show the true condition of affairs.³⁹ But a sale of stock should not be set aside for fraud-

³⁰ Hallidie v. First Federal Trust Co., — Cal. —, 171 Pac. 431; Smith v. Martin, — Vt. —, 106 Atl. 666.

³¹ Williams v. Beltz, — Del. —, 107 Atl. 298.

³² Arendt v. McConnell, — Cal. App. —, 183 Pac. 202.

³³ Shearer v. Farmers' Life Ins. Co., 262 Fed. 861.

³⁴ Smith v. Martin, — Vt. —, 106 Atl. 666.

³⁵ Cain v. Levy, 179 Ky. 32, 200 S. W. 326.

³⁶ Lentz v. Landers, — Ariz. —, 185 Pac. 821.

³⁷ Hutchinson v. Sperry, 261 Fed. 133.

³⁸ Schultz v. Andrews & Co., — Wis. —, 178 N. W. 459.

³⁹ Smith v. Martin, — Vt. —, 106 Atl. 666.

ulent representations as to the business of the corporation where the circumstances were such as to put any reasonable man upon inquiry as to the true state of the corporate affairs and where the buyer was in possession of the means and had at hand the opportunity to pursue the inquiry to a point where the precise facts would come into his possession.⁴⁰ The fact that a purchaser of stock takes an active part in the corporate business does not estop him from setting up fraud as a defense in an action against him for the price of the stock.⁴¹

§ 3877. — Necessity for injury. Injury is necessary to sustain an action for deceit, so that if the representations were not relied on no recovery can be had.⁴²

§ 3878. — Persons who may be held liable. Where one purchases stock in reliance on an untrue report by public accountants, the latter are not liable, there being no contract relations between them and the purchaser.⁴³

§ 3879. — Remedies for fraud—Rescission. Rescission is not the only remedy for fraud.⁴⁴ A complaint by a seller of stock to set aside his executed contract of sale for fraud is insufficient where it does not appear that an action at law for damages would be inadequate.⁴⁵

§ 3880. — — Restoration of the status quo. On rescinding, the seller must be put in statu quo.⁴⁶ A purchase of stock will not be rescinded for fraud where equity cannot be done by restoring the stock.⁴⁷ A purchaser of stock cannot rescind for fraud unless he returns or offers to return the stock, unless the stock was worthless.⁴⁸ A buyer of stock who desires to rescind

⁴⁰ *Hutchinson v. Sperry*, 261 Fed. 133.

⁴¹ *Rockhill v. Creer*, — Utah —, 189 Pac. 668.

⁴² See § 3875, *supra*.

⁴³ *Landell v. Lybrand*, 264 Pa. 406, 8 A. L. R. 461, 107 Atl. 783.

⁴⁴ *Rockhill v. Creer*, — Utah —, 189 Pac. 668.

⁴⁵ *Falk v. Hoffman*, 189 N. Y.

App. Div. 832, 179 N. Y. Supp. 428.

⁴⁶ *Barbour v. Poncelor*, — Ala. —, 83 So. 130; *Maginess v. Western Securities Corporation*, 38 Cal. App. 56, 175 Pac. 277, California statute.

⁴⁷ *Shearer v. Farmers' Life Ins. Co.*, 262 Fed. 861.

⁴⁸ *Brumbaugh v. Mellinger*, — Ind. App. —, 120 N. E. 676.

because of misrepresentations of the seller must return not only the stock but also dividends received on it.⁴⁹ On granting rescission to a purchaser of stock who had destroyed its value, he will be required to pay the actual value of the stock at the time of its purchase.⁵⁰

Even if certificates of stock have not been received, a buyer, on rescinding for fraud, should offer to restore the stock as distinguished from the certificates of stock.⁵¹

§ 3881. — Laches as a bar to rescission. Laches bars the right to rescind for fraud.⁵² Ordinarily, a purchaser of stock cannot rescind for fraud some six months after discovery of the fraud.⁵³

§ 3882. — Ratification or waiver as a bar to rescission. Ratification of a purchase of stock, after knowledge of the fraud of the seller, precludes the right to rescind for fraud.⁵⁴ Payment of assessments on stock does not necessarily bar the right to rescind for fraud.⁵⁵

There is no estoppel to rescind a purchase of stock for fraud because of a transfer of the business and assets of the corporation to the purchaser, where he had no knowledge of the fraud at the time of the transfer.⁵⁶

§ 3883. — Action for deceit—In general. The injured party may sue to recover damages for deceit.⁵⁷ A civil action lies for

⁴⁹ *Loomis v. Pease*, — Mass. —, 125 N. E. 177.

⁵⁰ *Shearer v. Farmers' Life Ins. Co.*, 262 Fed. 861.

⁵¹ *Maginess v. Western Securities Corporation*, 38 Cal. App. 56, 175 Pac. 277; *Brumbaugh v. Mellinger*, — Ind. App. —, 120 N. E. 676.

⁵² *Barbour v. Poncelor*, — Ala. —, 83 So. 130; *Munson v. Fishburn*, — Cal. —, 190 Pac. 808.

⁵³ *Maginess v. Western Securities Corporation*, 38 Cal. App. 56, 175 Pac. 277.

⁵⁴ *Maginess v. Western Securities Corporation*, 38 Cal. App. 56, 175 Pac. 277.

The right to revoke, for fraud, a purchase of stock, is waived where the purchase is perfected after knowledge of the fraud. *Thomas v. Birch*, 178 Cal. 483, 173 Pac. 1102.

⁵⁵ *Munson v. Fishburn*, — Cal. —, 190 Pac. 808.

⁵⁶ *Shearer v. Farmers' Life Ins. Co.*, 262 Fed. 861.

⁵⁷ Evidence admissible in action to recover damages for deceit in sale of stock, see *Smith v. Reynolds*, — Vt. —, 108 Atl. 697; *Smith v. Martin*, — Vt. —, 106 Atl. 666.

Where stockholders pool their stock, and one of them is induced

conspiracy to defraud by sale of stock to plaintiffs.⁵⁸ The measure of damages for fraud in inducing a purchase of stock is the difference between the amount paid and the real value of the stock;⁵⁹ and is governed by the law of the state where the sale was made.⁶⁰ Where a seller of stock sues for damages for fraud and deceit, he affirms the sale and cannot share in the benefits of a sale of the corporate property.⁶¹

§ 3884. — Waiver; limitations. Different statutes of limitation apply according to whether the action is one to rescind a purchase of stock for fraud or an action for damages by reason of such fraud.⁶² Limitations do not begin to run, where a sale of stock is based on misrepresentations, until the fraud is, or should have been, discovered.⁶³ Delay of over four years in suing for fraud inducing purchase of stock is not necessarily fatal.⁶⁴

§ 3885. Construction of contract in general.⁶⁵ A purchaser of stock is sometimes held, under his contract, to have assumed

to sell by false representations of the others as to value, damages are recoverable. *Frederick v. Brainard*, 32 Idaho 296, 182 Pac. 351.

⁵⁸ See *Dart v. McDonald*, 107 Wash. 537, 182 Pac. 628.

⁵⁹ *Reno v. Bull*, 226 N. Y. 546, 124 N. E. 144.

Method of fixing value of stock, in action for fraud, see *Armstrong v. Rachow*, 205 Mich. 168, 171 N. W. 389.

⁶⁰ *Williams v. Beltz*, — Del. —, 107 Atl. 298.

⁶¹ *Bollstrom v. Duplex Power Car Co.*, 208 Mich. 15, 175 N. W. 492.

⁶² *Texas Co.-Op. Inv. Co. v. Clark*, — Tex. Civ. App. —, 212 S. W. 245.

⁶³ *Williams v. Beltz*, — Del. —, 107 Atl. 298.

Cause of action for damages for fraud in sale of stock begins

to run when the fraud is discovered, notwithstanding the seller by words or action induced delay in suing. *Bain v. Lovejoy*, — Tex. Civ. App. —, 215 S. W. 984.

⁶⁴ *Armstrong v. Rachow*, 205 Mich. 168, 171 N. W. 389.

⁶⁵ Construction of particular contract to buy stock, see *Tolman v. Steele*, 209 Ill. App. 554.

Transaction as mere option to buy stock placed in escrow or as a sale of the stock, see *Hudson v. Riley*, 104 Kan. 534, 180 Pac. 198.

For an agreement held an optional and not an absolute agreement to buy stock, see *Western U. Tel. Co. v. Lange*, 248 Fed. 656.

Construction of agreement of stockholders with creditor of corporation to pay creditor or forfeit specified number of shares of stock, to obtain release of credi-

all the debts of the corporation.⁶⁶ Where a stockholder sells his stock, the good-will of the business goes with it.⁶⁷ Stockholders who pool their shares at the instance of a prospective purchaser are not joint adventurers.⁶⁸ Where an employee buys stock in his employer company on the implied understanding that he is to be employed for ten years, the company cannot retain the benefit of the stock transfer where the employment continues for only four years.⁶⁹ The words "actual book value," as used in a contract to purchase common stock at such value, mean the value of all the corporate assets, including good-will, and not any arbitrary or fictitious value brought about as a result of some system of bookkeeping; and it is immaterial that the corporation had ceased to carry "good-will" on its books as an asset, where without authority.⁷⁰ The words "interest in any incorporated company," as used in a power of attorney given to an associate, include power to sell the interest of the person giving the power in shares of stock standing in the name of another to execute a pooling arrangement.⁷¹

An order by plaintiff on a broker to deliver certain stock to another broker, with a written receipt by the latter for the stock, does not show an agreement by the latter to pay the value of the stock to the drawer of the order.⁷²

tor's lien, see *Leezer v. Fluhart*, 105 Wash. 618, 178 Pac. 817.

Construction of agreement to deliver stock or a named sum on surrender of certain other stock, as to sufficiency of demand for named sum only, see *Dozier v. National Borax Co.*, 35 Cal. App. 216, 170 Pac. 638.

Construction of contract, by which a corporation and some of its stockholders agreed to sell a portion of the stock to a stranger, as to how much stock each contracting stockholder should contribute to the sale, and as to who were bound by such contract, see *Vintroux v. Chilton*, — W. Va. —, 100 S. E. 496.

For article on agreement by re-

tiring stockholder as one in restraint of trade, see 8 Calif. L. Rev. 437-440.

⁶⁶ *R. R. Thompson Estate Co. v. Weinhard*, 247 Fed. 951; *Weinhard v. R. R. Thompson Estate Co.*, 242 Fed. 315.

⁶⁷ *Wylie v. Wylie Permanent Camping Co.*, — Mont. —, 187 Pac. 279.

⁶⁸ *McCord v. Martin*, — Cal. App. —, 191 Pac. 89.

⁶⁹ *Hancock v. Luke*, — Utah —, 173 Pac. 137.

⁷⁰ *Lane v. Barnard*, 103 N. Y. Misc. 707, 170 N. Y. Supp. 946.

⁷¹ *Warner v. Brown*, 231 Mass. 333, 121 N. E. 69.

⁷² *Noble v. Haff*, 172 N. Y. Supp. 139.

§ 3886. Admissibility of parol evidence. Parol evidence is admissible to show whether a contract was a sale of stock or a mortgage thereon or a pledge thereof.⁷³

§ 3887. Executed and executory contracts; when title passes. An unconditional offer to exchange corporate stock, where unequivocally accepted, passes the title on acceptance.⁷⁴

§ 3888. Conditions precedent and subsequent. Conditions precedent in a contract for sale of stock must, of course, be performed.⁷⁵ On selling stock, the seller may agree not to engage in the business for a certain time and to refrain for a specified time from certain things detrimental to the buyer.⁷⁶ One having an option to purchase stock need not do anything, in order to exercise the option, under ordinary circumstances, than to offer to pay the price fixed by the option.⁷⁷

§ 3889. Warranties, guaranties and special stipulations—Express warranties. Statements as to solvency of the corporation may amount to an express warranty that the company is in good financial condition.⁷⁸ For breach of warranty in the sale of all the capital stock of a corporation, the measure of damages is the difference between its value as warranted and its actual worth.⁷⁹

§ 3890. — Implied warranties. Where there is no fraud, the purchaser of overissued stock cannot hold the seller liable thereon, since the seller warrants only his own title and not the right of the corporation to issue the shares of stock.⁸⁰ On a sale

⁷³ Lyons v. Yielding, — Ala. —, 85 So. 21.

⁷⁴ Young v. New Pedrara Onyx Co., — Cal. App. —, 192 Pac. 55.

⁷⁵ Floyd v. Pugh, 201 Ala. 29, 77 So. 323.

⁷⁶ Feenaughty v. Beall, 91 Ore. 654, 178 Pac. 600.

⁷⁷ See Baker v. Mulrooney, 265 Fed. 529.

⁷⁸ Rockhill v. Creer, — Utah —, 189 Pac. 668.

⁷⁹ King v. Day, — Neb. —, 177 N. W. 160.

⁸⁰ The seller of stock does not impliedly warrant that the stock is not part of a fraudulent over-issue by the officers of the company. Leffingwell v. Evans, 185 Ky. 351, 216 S. W. 58.

The seller of stock does not impliedly warrant that the stock is not an overissue or fictitious, and is not liable to the purchaser although the corporation had no power to issue it. Randle v. Walker, — Ala. App. —, 84 So. 551.

of stock, where there is an express refusal to warrant the correctness of the books, there is no implied warranty that the books are correct.⁸¹

§ 3891. — Agreements by seller to repurchase or giving him option to do so, and the like.⁸² An option given the corporation to take over stock at par if the employee to whom given as a part of his salary should leave the service of the company is not in effect a forfeiture.⁸³ A contract for the sale of stock with an agreement to repurchase at the price paid, if the purchaser should become dissatisfied, is not invalid as unilateral nor as an option contract, nor within the statute of frauds where fully executed on one side and capable of being performed within one year.⁸⁴ A contract to repurchase stock is not within the statute of frauds where the liability to repurchase may be created at any time before the end of the year.⁸⁵

A contract to repurchase stock if the buyer should become dissatisfied is based on a sufficient consideration.⁸⁶ A fortiori, an agreement by a seller of stock to repurchase it at the end of four years is based on a good consideration where substituted for a contract to repurchase within a year.⁸⁷

⁸¹ *Luten v. Earles*, — Wash. —, 187 Pac. 349.

⁸² Construction of sale of shares with right of seller to repurchase, see *Hoberg v. McNeveins*, 169 Wis. 486, 173 N. W. 221.

Evidence admissible in action on a contract to repurchase stock sold, see *Bracey v. McGary*, 134 Md. 267, 106 Atl. 627.

Option given the corporation to repurchase stock sold an employee on his death or leaving the service, see *Hanson v. Brininstool*, — Cal. —, 178 Pac. 520.

Note on "Validity and construction of agreement by seller of corporate stock to repurchase on demand," see *Ann. Cas.* 1918 D 744.

⁸³ *Williams v. Maryland Glass*

Corporation, 134 Md. 320, 106 Atl. 755.

⁸⁴ *Hills v. Hopp*, 287 Ill. 375, 122 N. E. 510, aff'g 210 Ill. App. 365.

⁸⁵ *Ruzicka v. Lau*, 207 Ill. App. 326.

⁸⁶ *Hills v. Hopp*, 210 Ill. App. 365, aff'd 287 Ill. 375, 122 N. E. 510, holding also that it was immaterial that promisor who had a dominant interest in the corporation did not sell the stock directly to the buyer but transferred it to the corporation which thereafter sold it to the promisee.

⁸⁷ *Oncken v. Ehrler*, — Mo. App. —, 222 S. W. 1045.

A contract to forbear to sue upon an agreement to repurchase stock is a sufficient consideration

Where stock is sold with agreement to repurchase, a demand on the seller to repurchase is often a condition;⁸⁸ but if a seller of stock absolutely refuses to repurchase it as per his agreement, no tender nor formal demand is necessary before suing for breach of the agreement to repurchase.⁸⁹ A demand on the seller to repurchase stock, as per his agreement, need not be made on the precise date named in the contract;⁹⁰ but the option to resell or to repurchase cannot be exercised after the time limited by the agreement.⁹¹ An agreement whereby the seller of stock agrees to repurchase it at sale price plus interest, where silent as to time, means that the option to return the stock must be made within a reasonable time.⁹² Where a purchaser of stock is given the option to sell it to a third person at the end of a year for a certain price, he must execute his option within a reasonable time after the end of the year, and ten months is not a reasonable time.⁹³

Where a seller of stock breaches his agreement to repurchase it, the buyer may sue to recover the amount agreed to be paid for the stock and is not limited to an action for damages.⁹⁴ Of course if stock is sold on an agreement to return the price if the buyer is dissatisfied, and thereafter the buyer receives part of the price on account of liquidation of the stock, the buyer cannot recover the whole price from the seller.⁹⁵ Where the seller of stock agreed to resell it to a third person for the benefit of the purchaser, but rescinded the contract to sell to such third person, the purchaser can recover only the market value of the stock where it is not shown what would have been realized by a sale to such third person.⁹⁶ Where stock is sold under an agree-

to support a new agreement extending the time before demand for repurchase could be made. *Grasmuck v. Ehrler*, — Mo. App. —, 207 S. W. 287.

⁸⁸ See *Bracey v. McGary*, 134 Md. 267, 106 Atl. 622.

⁸⁹ *Vrba v. Krall*, — Iowa —, 175 N. W. 4.

⁹⁰ *Matson v. Bauman*, 139 Minn. 296, 166 N. W. 343.

⁹¹ *Kleinecke v. North Confidence Mining & Development Co.*, — Cal. App. —, 182 Pac. 313.

⁹² *McCollum v. Neimeyer*, — Ark. —, 219 S. W. 746. See *Hills v. Hopp*, 210 Ill. App. 365, aff'd 287 Ill. 375, 122 N. E. 510, holding delay of 17 months in particular case not too late.

⁹³ *McManaman v. Vickery*, — Cal. App. —, 183 Pac. 229.

⁹⁴ *Matson v. Bauman*, 139 Minn. 296, 166 N. W. 343.

⁹⁵ *Sawyer v. Huning*, — Ariz. —, 181 Pac. 172.

⁹⁶ *McCormick v. Badham*, 201 Ala. 210, 77 So. 736.

ment to repay part of the price, the obligation to repay cannot be defended against by showing that the purchaser made enough off an option on such stock to pay the original purchase price.⁹⁷ Where shares of stock were sold an employee under an agreement that if he died or left the service, shares not paid for should revert to the sellers, the reversion takes place on the occurrence of the event without any exercise of option.⁹⁸

Where one bought stock from an incorporator at less than half of par, under an agreement whereby the seller was to repurchase it for the sum paid at the end of two years if a certain profit had not then been made, it is no defense to an action at the end of the two years to recover back the sum paid that there was a violation of the constitutional provision requiring stock to be issued for money, labor done or property actually received, in that the company received from the incorporator for all its stock only properly mortgaged for its full value and that the purchaser knew that the equity of the incorporator was valueless.⁹⁹

§ 3892. — Guaranties and agreements by third persons.

Where an officer of a corporation, on selling stock, personally promises to refund the amount paid at any time, he is individually liable on such agreement.¹ A promise by a stockholder who transfers his stock to the corporation, to repurchase stock sold to employees when they quit, is based on a consideration where the stock is in fact the property of the stockholder and he derives direct personal benefit from the contract.²

§ 3893. Performance and breach generally.³ While equity abhors a forfeiture, a person cannot claim any title to stock where part payments were forfeited, where there was an offer to give stock or cash to the amount paid.⁴ One agreeing to sell or exchange one hundred shares of stock cannot evade liability

⁹⁷ *Abererombie v. Cullen*, 108 Wash. 515, 185 Pac. 595.

² *Ruzicka v. Lau*, 207 Ill. App. 326.

⁹⁸ *Hanson v. Brininstool*, — Cal. —, 178 Pac. 520.

³ Abandonment of option to purchase stock, see generally *Baker v. Mulrooney*, 265 Fed. 529.

⁹⁹ *Minge v. Clarke*, — Ala. —, 82 So. 439.

⁴ *Warfield v. Kelly*, 262 Pa.

¹ *Pfeiffer v. Mansbach*, 178 N. Y. Supp. 482.

482, 106 Atl. 72.

to transfer what he owns although less than one hundred shares.⁵ A seller of stock is liable for damages for failure to deliver the stock although the buyer purchased directly the stock which the seller intended to acquire.⁶

Leaving a certificate of stock at one's home for him is a sufficient delivery.⁷ Delivery of stock sold should be at the place of the seller, where there is no agreement or custom to the contrary.⁸

There is a fiduciary relationship where a customer deposits money with a stockbroker to buy securities.⁹

§ 3895. Tender and demand.¹⁰

§ 3896. Rescission of contract—Right to rescind in general.¹¹

An option to purchase stock, based on a cash consideration, is not subject to withdrawal by the owner of the stock.¹² Mistake is not ground for rescinding a sale of stock unless mutual.¹³ A sale of stock, where executed, will not be set aside for mutual mistake in that both seller and buyer relied on an erroneous inventory showing more corporate assets than there were.¹⁴ A purchaser of stock cannot rescind because of a mutual mistake of fact induced by misstatements in the corporate books as to the extent of the assets, where there was no fraud or inequitable conduct on the part of the seller and the means of information

⁵ *Young v. New Pedrara Onyx Co.*, — Cal. App. —, 192 Pac. 55.

⁶ *Gilbert v. Rosen*, 191 N. Y. App. Div. 87, 180 N. Y. Supp. 772.

⁷ *Lawrence v. Long Beach Pleasure Co.*, — Cal. App. —, 186 Pac. 606.

⁸ *Neer v. Lang*, 252 Fed. 575.

⁹ *Lipkien v. Krinski*, 192 N. Y. App. Div. 257, 182 N. Y. Supp. 454.

¹⁰ Tender of stock as condition precedent to action for price, see *Davies v. Price Merchants' Syndicate*, — Minn. —, 179 N. W. 215.

¹¹ What constitutes acceptance of rescission of exchange of stock, see *Young v. New Pedrara Onyx*

Co., — Cal. App. —, 192 Pac. 55.

Evidence admissible in action to recover stock which plaintiff claimed he was induced to transfer by false representations, see *Proctor v. Appleby*, — Wash. —, 188 Pac. 481.

Rule in Louisiana, under civil law, as to election of remedies where seller desires to rescind sale of stock, see *Atkins v. Garrett*, 252 Fed. 280.

¹² *Baker v. Mulrooney*, 265 Fed. 529.

¹³ *Reid v. Hughlett*, 135 Md. 181, 108 Atl. 477.

¹⁴ *Riviere v. Berla*, 89 N. J. Eq. 596, 106 Atl. 455.

were open to both alike.¹⁵ A sale of stock may be rescinded where the charter of the corporation had expired without the knowledge of the parties, but the lack of incorporation is waived by the purchaser organizing a new corporation with the same corporate name and assets.¹⁶

A bill to rescind a sale of stock for fraud and to restrain the receiver of the corporation from assessing or collecting any sum from complainant as a stockholder is not multifarious.¹⁷

§ 3897. — Limitations on the right to rescind.¹⁸ One who rescinds a stock contract must put the other in statu quo.¹⁹ Even if failure to deliver stock sold is ground for rescinding the sale, the sale cannot be rescinded for that reason after a delivery of the stock.²⁰ The fact that the seller of stock had, prior to suing the buyer for rescission of the contract for nonpayment of the purchase price, sold the certificate of stock to another, is no bar, at least in Louisiana, where plaintiff owned other stock more than sufficient to cover the shares sold to defendant.²¹ A seller of stock who sues to rescind for nonpayment of the purchase price need not, at least in Louisiana, tender payment of the dividends received by him on the stock put up as collateral to secure a note for the price.²²

§ 3898. Remedies for breach of the contract—In general. A purchaser of stock in a bank which was shortly afterwards declared insolvent may sue in equity to rescind the sale notwithstanding there is a concurrent remedy at law.²³ An action for damages for failure to deliver stock lies in favor of one who transferred patent rights to the corporation on the promise

¹⁵ Costello v. Sykes, 143 Minn. 109, 5 A. L. R. 250 with note, 172 N. W. 907.

“Rescission of sale of corporate stock on account of mutual mistake due to error in corporate books,” see note in 5 A. L. R. 255.

¹⁶ Scott v. Davis, 198 Mo. App. 512, 200 S. W. 723.

¹⁷ Heater v. Lloyd, — W. Va. —, 102 S. E. 228.

¹⁸ In case of fraud, see § 3880, supra.

¹⁹ Hancock v. Luke, — Utah —, 173 Pac. 137.

Restoring statu quo, as required by California statutes, see Fairchild v. Western Securities Corporation, 176 Cal. 742, 169 Pac. 363.

²⁰ Miley v. Heaney, 168 Wis. 58, 169 N. W. 64.

²¹ Atkins v. Garrett, 252 Fed. 280.

²² Atkins v. Garrett, 252 Fed. 280.

²³ Heater v. Lloyd, — W. Va. —, 102 S. E. 228.

of persons having stock in their control to transfer a certain amount of stock for such rights.²⁴ Where there were only two stockholders, and one sold his stock to the other with an agreement to sell goods and extend credit to the corporation, a breach of the agreement to sell goods creates a cause of action in favor of the purchaser of the stock as such and not in favor of the corporation.²⁵ The burden of proving a breach of a contract to sell stock is on plaintiff.²⁶

The measure of damages for breach of a contract to sell stock is sometimes expressly fixed by the contract itself which of course governs.²⁷ The damages for breach of a contract to deliver stock is the value of the stock at the time of the breach rather than its value at the date of the contract.²⁸

Where the purchaser of stock sues the seller in tort, there is not an election of remedies so as to bar an action on contract for rescission.²⁹ An election to sue for damages sustained by a purchase of stock precludes a suit to rescind the purchase and recover the amount paid.³⁰

§ 3899. — Specific performance—General principles. Specific performance of a contract to sell stock may be enforced where the remedy at law is inadequate,³¹ but it will be decreed only in exceptional cases,³² or in which the ends of justice require

²⁴ *Uhl v. Gayley*, 169 N. Y. Supp. 191.

²⁵ *Meyerson v. Franklin Knitting Mills*, 185 N. Y. App. Div. 458, 172 N. Y. Supp. 773.

²⁶ *Kunz v. Chouteau*, — Mo. App. —, 202 S. W. 443.

²⁷ *Friedman v. Padmore*, 103 Wash. 562, 175 Pac. 163.

²⁸ *Richards v. Vermilyea*, — Nev. —, 175 Pac. 188.

Measure of damages for breach of contract to sell stock of a corporation, where corporation sues, see *Middendorf, Williams & Co. v. Alexander Milburn Co.*, 134 Md. 395, 107 Atl. 7.

Proof of value of stock, see *Wohlgemuth v. Mendel*, 172 N. Y. Supp. 259.

²⁹ *Loomis v. Pease*, — Mass. —, 125 N. E. 177.

³⁰ *Issenhuth v. Kirkpatrick*, 258 Fed. 293.

³¹ *Mutual Oil Co. v. Hills*, 248 Fed. 257, where value of stock was not readily ascertainable and stock could not be bought in the market except at inconvenience and expense.

A bill in equity lies by the assignee of stock to compel a delivery of the certificates to him. *McGinniss v. First Nat. Bank*, 214 Ill. App. 295.

³² *Cape Girardeau-Jackson Interurban R. Co. v. Light & Development Co.*, 277 Mo. 579, 210 S. W. 361; *Nielsen v. Rebard*, — Nev. —, 183 Pac. 984; *Bartley v.*

it,³³ as when the value of the stock is not readily ascertainable or the stock cannot be had in the market except at great inconvenience and expense.³⁴ Shares of stock cannot be made the subject of specific performance unless they possess peculiar and unusual value.³⁵ Specific performance can be enforced only where the value of such stock is not easily ascertainable, or the stock cannot readily be obtained elsewhere or there is some particular and reasonable cause for the buyer requiring the stock itself to be delivered.³⁶ Specific performance of a contract to buy stock may be refused because of hardship to the buyer.³⁷ The seller of stock to be thereafter issued cannot enforce specific performance where he failed to tender the stock, after issuance, for eight months after a tender by the buyer of the price.³⁸

XXVI. PLEDGES, MORTGAGES AND LEASES OF STOCK

§ 3902. Shares of stock may be pledged. A stockbroker with whom stock is deposited has no authority to pledge it,³⁹ but a stockbroker may pledge stock of a margin customer.⁴⁰

§ 3903. Nature, essentials and validity of contract of pledge generally.⁴¹ Ownership shown on the face of the certificate,

Lindabury, 89 N. J. Eq. 8, 104 Atl. 333; Donovan v. Powers Film Products, 111 N. Y. Misc. 276, 181 N. Y. Supp. 157; Lane v. Barnard, 173 N. Y. Supp. 714; McCullough v. Clark, 81 W. Va. 743, 95 S. E. 787.

Specific performance by the corporation, to compel a delivery of stock subscribed for, is not allowable where there is an adequate remedy at law for damages. Toles v. Duplex Power Co., 202 Mich. 224, 168 N. W. 495.

³³ Amsler v. Cavitt, — Tex. Civ. App. —, 210 S. W. 766.

³⁴ Mutual Oil Co. v. Hills, 248 Fed. 257.

³⁵ Nielsen v. Rehard, — Nev. —, 183 Pac. 984.

³⁶ Hubbard v. George, 81 W. Va. 538, L. R. A. 1918 C 835, 94 S. E. 974.

³⁷ Bartley v. Lindabury, 89 N. J. Eq. 8, 104 Atl. 333.

³⁸ Kirkpatrick v. Lebus, 184 Ky. 139, 211 S. W. 572.

³⁹ Johnson v. Bixby, 252 Fed. 103, 1 A. L. R. 660.

⁴⁰ In re J. C. Wilson & Co., 252 Fed. 631.

⁴¹ Where stock issued after the charter expired was pledged, rights of pledgor, on failure to make payments, considered in Scott v. Davis, 198 Mo. App. 512, 200 S. W. 723.

An owner of stock who lent it for use as security, held to have ratified an unauthorized pledge

coupled with the owner's signature to the transfer in blank preceded by the words "as collateral" is sufficient to show not merely to the first pledgee but also to subsequent pledgees and to an associate of the pledgor, that the original transfer by the owner to the pledgor was conditional.⁴²

§ 3904. Pledges, mortgages and sales distinguished. That a transfer of stock is called an assignment and sale does not affect its true character as a pledge.⁴³ A stockholder who advances part of the money in buying stock for a customer, and retains the stock as security, is a pledgee.⁴⁴

§ 3907. Necessity for registration. A transfer on the books is not necessary to a valid pledge of stock.⁴⁵ If shares of stock remain in the name of the pledgor on the books of the corporation, and the pledgee wrongfully uses the certificate by repledging it, the second pledgee who takes it in good faith and without notice of the owner's claim is entitled to retain it as security for the debt for which pledged.⁴⁶

Under the Colorado statute invalidating pledges of stock unless a memorandum is made on the books of the company showing to whom and for what amount the stock has been pledged, a pledge is invalid as against an execution sale of the stock where the pledgee failed for two years to notify the corporation of the pledge and then did not state the amount for which the stock was pledged.⁴⁷

§ 3908. Scope of lien. A pledge of stock covers subsequent loans by the pledgee to the pledgor, although the pledgee knew of a third person's equity in the stock, where the subsequent loans

by the borrower, in *Schwartz v. Clark*, — W. Va. —, 103 S. E. 47.

Broker as pledgee of stock, see *Hoppenstedt v. Amy*, 174 N. Y. Supp. 742.

⁴² *Crosby v. Simpson*, — Mass. —, 125 N. E. 616.

⁴³ *Galland Bros. Corporation v. Rundel*, 108 Wash. 5, 182 Pac. 933.

⁴⁴ *Duel v. Hollins*, 241 U. S.

523, 60 L. Ed. 1143; *Tuckerman v. Mearns*, 262 Fed. 607.

⁴⁵ *Young v. New Pedrara Onyx Co.*, — Cal. App. —, 192 Pac. 55.

⁴⁶ *Hellman Commercial Trust & Savings Bank v. Armstrong*, 39 Cal. App. 483, 179 Pac. 432, following *Fowles v. National Bank*, 167 Cal. 653, 140 Pac. 271.

⁴⁷ *Hexter v. Shahan*, — Colo. —, 180 Pac. 92.

were practically forced ones to protect the original loan.⁴⁸ If two certificates of stock are pledged and a new certificate is procured to replace one sold by mistake, the new certificate is subject to the lien although the other certificate was ample security.⁴⁹

§ 3909. Effect of pledge on title and rights of pledgor. Title to stocks bought on margin is in the brokers until payment therefor or an offer of payment.⁵⁰ So the legal title to stock deposited as margin is in the broker.⁵¹

§ 3910. Title and rights of pledgee—In general.⁵² A pledgee of stock cannot assert ownership thereof in a person other than the pledgor, where such person has made no claim or demand.⁵³ That certificates of stock pledged by the secretary were signed by the secretary is not notice putting the pledgee on inquiry as to their validity.⁵⁴

§ 3911. — Right to transfer of stock on corporate books.⁵⁵

§ 3912. — Right to use pledged stock. Stock put up as margin cannot be disposed of by the broker.⁵⁶ A broker converts stock carried on margin where he takes it over for his own account, in breach of an agreement with the customer.⁵⁷ A broker who holds unindorsed stock as collateral has a right to rehypothecate it, without indorsement, to the extent of his interest therein.⁵⁸ The rights inter se of customers whose

⁴⁸ *Citizens' Sav. Bank v. Mack*, — Cal. —, 180 Pac. 618.

⁴⁹ *Leishing v. Van Buren*, 170 N. Y. Supp. 193.

⁵⁰ *Crehan v. Megargel*, — Mass. —, 126 N. E. 477; *Hall v. Paine*, 230 Mass. 62, 119 N. E. 664.

⁵¹ *Crehan v. Megargel*, — Mass. —, 126 N. E. 477.

⁵² Pledge of stock as collateral to a note, construction in general, see *Commercial Nat. Bank v. May*, — Iowa —, 174 N. W. 646.

Pledgee of stock as security for an antecedent debt as a bona fide purchaser for value, see note in 9 A. L. R. 1619, annotating

Millard v. Green, — Conn. —, 9 A. L. R. 1610, 110 Atl. 177.

⁵³ *Bumiller v. Bumiller*, 179 Cal. 119, 175 Pac. 897.

⁵⁴ *Greensburg Title & Trust Co. v. Aspinwall-Delafield Co.*, 266 Pa. 160, 109 Atl. 631.

⁵⁵ Transfer of pledged stock on books of corporation as a conversion, see *Foto v. Bussell*, — Cal. App. —, 187 Pac. 432.

⁵⁶ *Crehan v. Megargel*, — Mass. —, 126 N. E. 477.

⁵⁷ *Hall v. Paine*, 230 Mass. 62, 119 N. E. 664.

⁵⁸ *Leishing v. Van Buren*, 170 N. Y. Supp. 688.

securities have been repledged by the broker often involve complicated questions.⁵⁹ Under Massachusetts law, a customer of a stockbroker who turns over stock to be used as collateral for margin trading, does not lose title to the pledged stock, and if the broker repledges it and defaults, the customer is entitled to any balance after the sale of collateral to satisfy the obligation of the broker.⁶⁰

If the pledgee of stock executes a separate blank assignment of the stock, it merely transfers the title of the pledgee, even though the owner assents to such assignment.⁶¹

A corporation which is the pledgee of its own stock has no authority, as against the pledgor, to sell the stock with accrued dividends represented by checks at the time in the possession of the pledgee.⁶²

§ 3913. — Negligence or misconduct in use or care of stock. Stockbrokers who carry stocks on margins must have them under control and available for delivery.⁶³

§ 3915. — Right to sue to preserve security or for damages. A pledgee of stock may sue in equity to protect his rights.⁶⁴ If a pledgee has a lien or rights superior to the lien of an execution, he may enjoin the sale under execution pending a bill quia timet.⁶⁵

§ 3918. — Title or lien of pledgee as against third persons—
In general. A transferee of stock with actual or constructive notice of a prior pledge of the stock takes subject thereto.⁶⁶ So a pledge of stock takes precedence over a subsequent execution sale as the property of the pledgor.⁶⁷ The pledgee of stock

⁵⁹ See note on this subject in 1 A. L. R. 664, annotating *Johnson v. Bixby*, 252 Fed. 103, 1 A. L. R. 660.

⁶⁰ *In re Gay & Sturgis*, 251 Fed. 420.

⁶¹ *Crosby v. Simpson*, — Mass. —, 125 N. E. 616.

⁶² *Brightson v. Clafin*, 225 N. Y. 469, 122 N. E. 458, rev'g 173 N. Y. App. Div. 967, 159 N. Y. Supp. 1102.

⁶³ *In re Shea*, 245 Fed. 363.

⁶⁴ *First Nat. Bank v. Multnomah State Bank*, 87 Ore. 423, 170 Pac. 534.

⁶⁵ *Lambert v. Huff, Andrews & Thomas Co.*, 82 W. Va. 362, 1 A. L. R. 650, 95 S. E. 1031.

⁶⁶ *Young v. New Pedrara Onyx Co.*, — Cal. App. —, 192 Pac. 55.

⁶⁷ *Bank of Napa v. Ferguson Burns Estate*, — Cal. App. —, 192 Pac. 66.

takes title subject to the title of the pledgor, and his rights are superior to those of a third person having a beneficial interest therein.⁶⁸ A pledgee of stock from the apparent owner is not chargeable with knowledge of a limitation placed on it by the real owner or of any secret agreement relating to the use which might be made of the stock by the holder.⁶⁹ The rights of a pledgee of stock to foreclose his lien are superior to those of the true owner who had indorsed and delivered the certificates in trust to one who had fraudulently pledged them.⁷⁰ Notice of a claim to stock, before taking the stock as a pledge, makes the title of the pledgee subject to such claim.⁷¹

A pledgee of stock for a pre-existing debt is not a bona fide purchaser for value, in some jurisdictions.⁷²

§ 3919. — Marshalling securities. Where money is loaned on stock as security, as well as a mortgage, the lender is properly required to resort to the mortgage before selling the pledge of stock, where a third person had equities in the pledged stock.⁷³

§ 3925. Rights and remedies on default—Sale of stock—Right to sell. A pledgee of stock, on default, may sell it only so far as necessary to satisfy his claim.⁷⁴ He may be enjoined from selling it, in a proper case.⁷⁵ His right to sell at any time is waived by granting an indefinite extension of time to the pledgor.⁷⁶ A sheriff's sale of stock to satisfy a pledge cannot be collaterally attacked.⁷⁷

⁶⁸ Iowa Securities Corporation v. Ridgewood Nat. Bank, 106 N. Y. Misc. 335, 175 N. Y. Supp. 776.

⁶⁹ Spellacy v. Young, — Cal. App. —, 186 Pac. 368.

⁷⁰ Swigart v. Stoops, 204 Ill. App. 194.

⁷¹ Western Nat. Bank of Hereford v. Walker, — Tex. Civ. App. —, 206 S. W. 544.

⁷² Millard v. Green, — Conn. —, 9 A. L. R. 1610, 110 Atl. 177.

⁷³ Citizens' Sav. Bank v. Mack, — Cal. —, 180 Pac. 618.

⁷⁴ Johnson v. Bixby, 252 Fed. 103.

Right of pledgee of stock to

sell it under Louisiana statutes, see Atkins v. Garrett, 252 Fed. 280.

What constitutes estoppel or waiver in case of wrongful sale by pledgee of pledged stock, see Brightson v. Clafin, 225 N. Y. 469, 122 N. E. 458, rev'g 173 N. Y. App. Div. 967, 159 N. Y. Supp. 1102.

⁷⁵ Clayton v. Smith, 131 Md. 562, 102 Atl. 925.

⁷⁶ Musser v. McCormick & Co., — Utah —, 192 Pac. 1052.

⁷⁷ Safford v. Tibbetts, 104 Kan. 224, 178 Pac. 618.

§ 3926. — — **Demand and notice.** In the absence of statute, a pledgee must give public notice of a sale of the stock and it is not sufficient to merely mail a notice to the pledgor.⁷⁸ But demand or notice is not necessary before the sale of pledged stock, where waived by the provisions of a note given for the debt.⁷⁹

§ 3927. — — **Manner of sale in general.** Stock sold by a pledgee need not bring the actual market price, in order to be valid.⁸⁰

§ 3930. — — **Right of pledgee to purchase.** A pledgee may bid at his own sale if so authorized by the pledgor.⁸¹

§ 3931. — **Foreclosure in equity.** Equity has jurisdiction of a suit by a pledgee of stock against a subsequent pledgee in possession of the certificate to adjudicate the rights of the parties and decree a sale and distribution of the proceeds.⁸²

§ 3934. — **Effect of sale or foreclosure; surplus or deficiency.** A purchaser of stock at a pledgee's sale, with knowledge of the want of power to make the pledge, cannot hold the stock as against the true owner, after reimbursement.⁸³

§ 3936. — **Redemption—Right to redeem.** Under the California statutes, a third person who has acquired an interest in stock pledged, may redeem from the lien of the pledge, and if the pledgee refuses to deliver the stock he is guilty of conversion.⁸⁴

§ 3940. — Effect of bankruptcy of pledgee.⁸⁵

⁷⁸ Richardson v. Foster, 100 Wash. 57, 170 Pac. 321.

⁷⁹ Williams v. Yountz, — Cal. —, 172 Pac. 383.

⁸⁰ Western Securities Co. v. Silver King Consol. Min. Co., — Utah —, 192 Pac. 664.

⁸¹ Western Securities Co. v. Silver King Consol. Min. Co., — Utah —, 192 Pac. 664.

⁸² Security Realty Inv. Co. v. Lewis, Hubbard & Co., — W. Va. —, 102 S. E. 702.

⁸³ Kay v. Piney Coal & Coke Co., — W. Va. —, 99 S. E. 501.

⁸⁴ Bumiller v. Bumiller, 179 Cal. 119, 175 Pac. 897.

⁸⁵ Rights of customers on bankruptcy of stockbroker, where stock of customers had been

§ 3942. — Subrogation. Where corporate stock owned by one was put up as collateral for a loan to two, and the nonowner paid the debt, he was subrogated to the rights of the pledgee.⁸⁶

§ 3943. Remedies of pledgor for conversion or breach of contract.⁸⁷ A broker holding stock purchased, as security for margins, is a pledgee of the stock and guilty of conversion where he refuses to deliver it on tender of the amount due.⁸⁸ Where a certificate of stock is pledged with a trustee to secure a note, but the payee of the note is not a party to the agreement, the payee is not liable for loss of the stock.⁸⁹ An unauthorized sale of stock by the pledgee does not defeat the lien of the pledge, and hence if the value of the stock is less than the debt no recovery can be had because of such sale.⁹⁰ In an action for conversion of pledged stock by a wrongful sale by the pledgee, the damages should be reduced by subtracting the amount of the debt for which the stock was pledged.⁹¹

§ 3944. Mortgage of shares of stock. A bill of sale of corporate stock is a mortgage, regardless of the wording of the contract, where given to secure a debt.⁹² An agreement whereby one of several prospective bidders bids for all, at a foreclosure sale of shares of stock, is not necessarily ground for setting aside the sale as chilling bidding, unless it was entered into with the object of suppressing competition or accomplishment of some other fraud.⁹³

pledged without authority, see *In re J. C. Wilson & Co.*, 252 Fed. 631.

⁸⁶ *Rhea v. Maxwell*, 111 S. C. 460, 98 S. E. 795.

⁸⁷ Conversion of customer's stock by stockbroker, and rights of customer where broker becomes a bankrupt, see *In re J. C. Wilson & Co.*, 252 Fed. 631.

⁸⁸ *Drake v. Hodgson*, 192 N. Y. App. Div. 676, 183 N. Y. Supp. 486.

⁸⁹ *Powell v. Hookerton Terminal Co.*, — N. C. —, 103 S. E. 892.

⁹⁰ *Musser v. McCormick & Co.*, — Utah —, 192 Pac. 1052.

⁹¹ *Brightson v. Claffin*, 225 N. Y. 469, 122 N. E. 458.

⁹² *Lyons v. Yielding*, — Ala. —, 85 So. 21.

Transfer of shares of stock as constituting a mortgage or a pledge, see *Oden v. Vaughn*, — Ala. —, 85 So. 779.

⁹³ *Schmitt v. Schmitt*, 169 Wis. 28, 171 N. W. 655.

XXVII. GIFTS OF STOCK

§ 3946. General principles.⁹⁴ An agreement to make a gift of all future dividends on stock cannot be enforced.⁹⁵ Stockholders may donate part of their stock back to the corporation, and however technically imperfect the form of the donation may be, it is valid against a collateral attack.⁹⁶

§ 3947. Necessity for and sufficiency of delivery. The fact that stock stands in the name of a certain person does not make it subject to execution as his property where it was never delivered to him and there was merely an intent of the real owner to make a gift at a future time.⁹⁷ The certificate of stock need not itself be delivered, to make a valid gift.⁹⁸ Delivery of certificates of stock without indorsement is sufficient to constitute a valid gift if the intent of the donor was to pass title at once.⁹⁹

§ 3949. Transfer of title, dominion and control. There may be a valid gift of stock although it is not to become effective until after the death of the donor.¹

XXVIII. MEMBERSHIP IN CORPORATIONS

§ 3952. Acquisition of membership—Necessity for contract. A person may become a member by signing a pledge card, so as to be liable for dues provided for by the by-laws.²

§ 3963. Loss of membership—Disfranchisement or expulsion of members—Particular grounds. The Chicago Board of Trade

⁹⁴ Transaction as gift of stock, see *Washington Trust Co. v. Thomas*, — R. I. —, 107 Atl. 203.

⁹⁵ *Banner Window Glass Co. v. Barriat*, — W. Va. —, 102 S. E. 726.

⁹⁶ *Hasson v. Koerberle*, — Cal. —, 181 Pac. 387.

⁹⁷ *Fink v. Schleuter*, 206 Ill. App. 159.

⁹⁸ *In re Cohn*, 187 N. Y. App. Div. 392, 176 N. Y. Supp. 225.

⁹⁹ *Reinhard v. Sidney B. Roby Co.*, 110 N. Y. Misc. 152, 179 N. Y. Supp. 781.

¹ *In re Humphrey's Estate*, 191 N. Y. App. Div. 291, 181 N. Y. Supp. 169. See also *Orton v. Tannenbaum*, 110 N. Y. Misc. 128, 181 N. Y. Supp. 84.

² *Mechanicville War Chest v. Butterfield*, 110 N. Y. Misc. 257, 181 N. Y. Supp. 428.

has power to provide by by-law for forfeiture of membership for fraud of the member in securing his acceptance as a member.³

§ 3964. — — Good faith. A board of directors of a live stock exchange are not liable in damages for acts in connection with charges against a member of the exchange, where acting in the exercise of judicial authority, regardless of their motives.⁴

§ 3968. — — Review by the courts. An expelled member who has acquired property rights may resort to the courts in case of wrongful expulsion.⁵ An expulsion of a member will be set aside by the courts where he is not given a fair hearing as required by the regulations,⁶ but the courts will not review the expulsion of a member of an incorporated club so far as the wisdom or expediency thereof is concerned.⁷ A member of a beneficial society wrongfully expelled may resort to the courts only when property rights are involved.⁸ Mandamus does not lie to compel reinstatement on the ground of mere informalities in the proceedings resulting in the expulsion.⁹

§ 3969. — — Remedies for wrongful expulsion. Suspension of a branch lodge which in effect suspends its members may be enjoined where unlawful or arbitrary.¹⁰

§ 3970. — — Necessity for exhausting remedies within the organization. A bill to reinstate an expelled member does not lie where remedies available within the corporation are not first availed of.¹¹ The courts will not reinstate an expelled member

³ *Turner v. Board of Trade*, 244 Fed. 108.

⁴ *Melady v. South St. Paul Live Stock Exchange*, 142 Minn. 194, 171 N. W. 806.

⁵ *Grand Lodge, K. P. v. Taylor*, — Fla. —, 84 So. 609.

⁶ *Universal Lodge No. 14 Free & Accepted Masons of City of Annapolis v. Valentine*, 134 Md. 505, 107 Atl. 531.

⁷ *Richards v. Morison*, 229 Mass. 458, 118 N. E. 868.

⁸ *Grand Lodge v. Taylor*, — Fla. —, 84 So. 609.

⁹ *People ex rel. Mermel v. Polish Nat. Alliance*, 210 Ill. App. 156.

¹⁰ *Gardner v. Newbert*, — Ind. App. —, 128 N. E. 704.

¹¹ *Most Worshipful. United Grand Lodge of Free & Accepted Masons of Maryland, Inc. v. Lee*, 131 Md. 681, 103 Atl. 88; *Acri v. Bruscia*, 265 Pa. 384, 108 Atl. 717.

unless he first has sought relief as provided for by the rules of the company.¹²

**XXIX. CONTROL OF CORPORATION BY STOCKHOLDERS OR MEMBERS;
POWER OF THE MAJORITY**

A. General Rules

§ 3972. Powers and duties of majority—In general.¹³ A majority stockholder may control the business and dictate its affairs,¹⁴ but minority shareholders cannot be forced by the majority to sell their stock.¹⁵

§ 3973. — Majority stockholders as trustees for minority. Majority stockholders, in controlling the corporation, occupy a fiduciary relation towards the minority,¹⁶ as much so as the corporation itself or its officers and directors.¹⁷ Where a corporation is sought to be held liable, as majority stockholder, for assets which it has not shared with the minority, fraud or mismanagement is not necessarily involved.¹⁸ Where certain stockholders wrongfully take control of and sell corporate property, under a fraudulent contract, they become trustees of the other stockholders and chargeable with the market price of the property at the time they sold it.¹⁹

§ 3982. Extent of stock holdings as affecting rights and remedies. One holding a very small amount of stock may nevertheless bring a stockholders' suit.²⁰ A minority stockholder, although his interest is only one per cent of the total stock,

¹² State ex rel. Cammann v. Tower Grove Turn Verein, — Mo. App. —, 206 S. W. 242.

¹³ See also § 1754, supra.

¹⁴ Kahan v. Alaska Junk Co., — Wash. —, 189 Pac. 262.

¹⁵ Brown v. British Abrasive Wheel Co., Ltd., [1919] 1 Ch. Div. 290.

¹⁶ Southern Pac. Co. v. Bogert, 250 U. S. 483, 63 L. Ed. 1099, modifying 244 Fed. 61; Kavanaugh v.

Kavanaugh Knitting Co., 226 N. Y. 185, 123 N. E. 148.

¹⁷ Southern Pac. Co. v. Bogert, 250 U. S. 483, 63 L. Ed. 1099.

¹⁸ Southern Pac. Co. v. Bogert, 250 U. S. 483, 63 L. Ed. 1099, modifying 244 Fed. 61.

¹⁹ Fredenhall v. Shroder, — Cal. App. —, 188 Pac. 580.

²⁰ General Inv. Co. v. Lake Shore & M. S. Ry. Co., 250 Fed. 160, 173, aff'g 226 Fed. 976.

is entitled to relief where corporate assets are dissipated.²¹ However, the fact that other minority stockholders do not join in a stockholders' suit attacking acts of the majority is worthy of consideration.²²

B. Particular Forms of Corporate Control

§ 3984. In general. The doctrine by which the holders of a majority of the stock who dominate the corporate affairs are trustees for the minority, is based on the fact of control of the common property, and is not affected by the particular means by which or manner in which the control is exercised.²³

§ 3988. Corporation as majority stockholder—In general. A corporation is liable to minority stockholders of another corporation, for its acts as majority stockholder to the detriment of minority stockholders, although it really was not a stockholder, where it controlled a company which held a majority of such stock and acted under its orders.²⁴

§ 3990. — Holding companies. A holding company is not merged in a subsidiary company and does not lose its corporate identity.²⁵ Courts will not hesitate to grant merited relief where a subsidiary company becomes bankrupt, so far as the holding company is concerned.²⁶

C. In What Cases Minority May Resort to Courts

§ 3991. General rule.²⁷ Equity will protect a minority stockholder "against the acts or threatened acts of the board of directors or of the managing stockholders of the corporation, which violate the fiduciary relation and are directly injurious to the stockholders."²⁸ Minority stockholders may sue to

²¹ *Gordon v. Brucker*, 208 Ill. App. 188.

²² *Presidio Min. Co. v. Overton*, 261 Fed. 933.

²³ *Southern Pac. Co. v. Bogert*, 250 U. S. 483, 63 L. Ed. 1099.

²⁴ *Southern Pac. Co. v. Bogert*, 250 U. S. 483, 63 L. Ed. 1099, modifying 244 Fed. 61, which aff'd 226 Fed. 500.

²⁵ *City of Holland v. Holland City Gas Co.*, 257 Fed. 679, and see §§ 22, 45, *supra*.

²⁶ *City of Holland v. Holland City Gas Co.*, 257 Fed. 679.

²⁷ See *Kremer v. Public Drug Co.*, 41 S. D. 365, 170 N. W. 571.

²⁸ *Kavanaugh v. Kavanaugh Knitting Co.*, 226 N. Y. 185, 123 N. E. 148, rev'g on other grounds

terminate a contract giving a perpetual and exclusive option to another to purchase stock of the corporation, where prejudicial to such minority stockholders.²⁹

Where the stock of a corporation is owned by two persons, and on its ceasing to do business the majority stockholder proceeds to convert all the corporate property to his own use, the minority stockholder may sue the majority stockholder, making the corporation a party defendant, and a judgment may be entered against the majority stockholder for his aliquot part of the funds due the corporation.³⁰

§ 3992. Intra vires acts where there is no bad faith—Rule stated.³¹ The court will not by mandatory injunction vest the exclusive management in a minority stockholder and thereby oust the directors put in by the majority stockholder, merely because if a certain contract between the two stockholders had been carried out it would have been highly beneficial to both.³²

§ 3997. Bad faith or fraud—Rule stated. Minority stockholders are entitled to relief where the managing officers are running the corporation solely for the benefit of another corporation.³³ Where majority stockholders, by deception as to profits, induce the minority to exchange common for preferred stock, the majority can be compelled to return such common stock and account for the profits.³⁴

§ 3998. — Misappropriation or diversion of corporate funds or assets. Majority stockholders are liable to account for refusing to make a pro rata distribution of proceeds of sales of corporate property among minority stockholders, although not guilty of any fraud or mismanagement.³⁵ It has been held that a minority stockholder may sue and recover from a majority

184 N. Y. App. Div. 650, 172 N. Y. Supp. 376.

²⁹ Kingston v. Home Life Ins. Co., — Del. —, 104 Atl. 25, aff'g 101 Atl. 898.

³⁰ Dill v. Johnston, — Okla. —, 179 Pac. 608.

³¹ See § 4065, *infra*.

³² Cuppy v. Ward, 187 N. Y.

App. Div. 625, 176 N. Y. Supp. 233.

³³ Bernheim v. Louisville Property Co., 185 Ky. 63, 214 S. W. 801.

³⁴ Macgill v. Macgill, 135 Md. 384, 109 Atl. 72.

³⁵ Southern Pac. Co. v. Bogert, 250 U. S. 483, 63 L. Ed. 1099.

stockholder his aliquot part of the assets of the corporation diverted by such majority stockholder, at least where the corporation is a two man corporation; and it is not necessary to render judgment in favor of the corporation or to have the corporation sue.³⁶

§ 3999. — Division of assets. If majority stockholders procure a sale of the corporate property and themselves acquire it, the minority cannot be excluded from a fair participation in the proceeds of the sale.³⁷

E. Rights of Minority as to Sale, Exchange or Lease of Corporate Property

§ 4010. In general. Where, through control by majority stockholders, a sale of the corporate property is made and the property acquired by the majority, the minority cannot be excluded from a fair participation in the fruits of the sale.³⁸

§ 4011. Power of majority to dispose of all of corporate property—General rule.³⁹

§ 4014. — Where sale expressly authorized by statute.⁴⁰

§ 4016. Taking stock or bonds of another corporation.⁴¹

F. Statutes Requiring Consent of Certain Per Cent of Stock

§ 4018. General considerations.⁴²

G. Defenses Against Minority Stockholders

§ 4023. Laches, ratification and estoppel.⁴³ Minority stockholders are estopped to attack the validity of a corporate lease

³⁶ Dill v. Johnston, — Okla. —, 179 Pac. 608.

³⁷ Southern Pac. Co. v. Bogert, 250 U. S. 483, 63 L. Ed. 1099.

³⁸ Southern Pac. Co. v. Bogert, 250 U. S. 483, 63 L. Ed. 1099, modifying 244 Fed. 61.

³⁹ See § 1206 et seq., supra.

Purchase by majority stockholders, see § 4035, infra.

⁴⁰ See § 1210, supra.

⁴¹ See § 1211, supra.

⁴² See § 1736, supra.

⁴³ For numerous applications of rule as to laches, see Baillie v. Columbia Gold Min. Co., 86 Ore. 1,

many years after its execution, where they had had knowledge thereof.⁴⁴ Laches precludes an attack by minority stockholders on a sale by the corporation of all its property, where, with knowledge, nothing is done until the purchasing corporation is a business success.⁴⁵ Delay of over two years in attacking a sale of all the corporate assets for fraud has been held not laches on the part of a minority stockholder, where it was some time before he had full knowledge of the facts.⁴⁶ Lapse of over twenty years is not laches on the part of minority stockholders, where most of the time they have been unsuccessfully seeking to discover the appropriate remedy by various actions, and defendant was not prejudiced by the delay.⁴⁷

H. Remedies of Minority Stockholders

§ 4025. In general. Minority stockholders are entitled to an accounting from majority stockholders who freeze them out by voting a dissolution of the corporation and then purchasing the assets through a new corporation.⁴⁸ Where there is only one stockholder objecting to the transfer of the corporate assets to a new company, and he sues for a receiver and a distribution of the corporate assets, the court properly gives the new company the right to retain such assets on paying complainant the value of his stock.⁴⁹

§ 4027. Statutory provisions for compensating dissenting stockholders. The benefit of the statute as to appraisement of stock of nonconsenting minority stockholders is not confined to stockholders of record.⁵⁰ A dissenting stockholder who seeks an appraisement of the value of his stock on a sale of all or practically all the corporate property, may compel a purchase of his stock at the appraised value although the sale was void-

166 Pac. 965, and also § 4072 et seq., *infra*.

⁴⁴ *Elder v. Western Min. Co.*, 263 Fed. 414.

⁴⁵ *Carrier v. Dixon*, 142 Tenn. 122, 218 S. W. 395.

⁴⁶ *Tierney v. United Pocahontas Coal Co.*, — W. Va. —, 102 S. E. 249.

⁴⁷ *Southern Pac. Co. v. Bogert*,

250 U. S. 483, 63 L. Ed. 1099, modifying 244 Fed. 61.

⁴⁸ *Major v. American Malt & Grain Co.*, 110 N. Y. Misc. 132, 181 N. Y. Supp. 152.

⁴⁹ *Kremer v. Public Drug Co.*, — S. D. —, 170 N. W. 571.

⁵⁰ *In re Rowe*, 107 N. Y. Misc. 549, 176 N. Y. Supp. 753.

able at his election because consent thereto was not given at a stockholders' meeting.⁵¹ In Ohio, an award of arbitrators in favor of dissenting stockholders, on a sale of all the corporate assets, as to the amount which should be paid such dissenters for their stock, may be set aside where legal defects appear on the face of the award.⁵² In New York, so far as the "Stock Corporation Law" is in conflict with the "Transportation Corporations Law" as to appraisement of the value of stock of dissenting stockholders of a telephone company, on a sale of all its property, the latter must prevail.⁵³

In case of national banks, the federal statutes provide that a stockholder who does not assent to an amendment of the charter extending corporate existence, may, on giving notice, obtain the value of his shares.⁵⁴

XXX. DEALINGS BETWEEN CORPORATION AND ITS STOCKHOLDERS AND DEALINGS OF STOCKHOLDERS WITH CORPORATE PROPERTY

§ 4030. Validity of contracts between corporation and stockholder—General rule. Stockholders may contract with the corporation and so become a creditor and entitled to all the rights and remedies of creditors.⁵⁵ However, the rule that a stockholder may deal with a corporation the same as any stranger is subject to the qualification that the transaction be free from fraud and not unfair to the corporation itself.⁵⁶

§ 4032. — Purchase, sale or lease. A sale of all the property of a corporation to part of the stockholders cannot be complained of where fair and just, merely because of the relationship of the purchaser.⁵⁷

⁵¹ *In re Drosnes*, 187 N. Y. App. Div. 425, 175 N. Y. Supp. 628 (but see dissenting opinion of Justice Page).

⁵² *Hoffard v. Williams Shoe Co.*, 95 Ohio St. 376, 117 N. E. 17.

⁵³ *In re Bronson*, 164 N. Y. Supp. 179.

⁵⁴ *Conway v. First Nat. Bank*, 256 Fed. 277, discussing question of notice.

⁵⁵ *Merchants' Bank of Mobile v. Zadek*, — Ala. —, 84 So. 715.

Construction of agreement between corporation and its stockholders for services, see *Gay v. American Trading Co.*, 179 Ky. 94, 200 S. W. 353.

⁵⁶ *Smith v. Smith*, — Tex. Civ. App. —, 213 S. W. 273.

⁵⁷ *Carrier v. Dixon*, 142 Tenn. 122, 218 S. W. 395.

§ 4033. — Guaranty of corporate debts.⁵⁸ Of course even a minority stockholder may make himself personally liable for work performed on buildings owned by the corporation, as an original promisor as distinguished from a guarantor.⁵⁹

§ 4035. — Frauds upon other stockholders. Where the purchaser of all the assets of a corporation is another company owned entirely by the majority stockholder of the seller, the utmost good faith is required to prevent the setting aside of the sale at the suit of a minority stockholder of the seller.⁶⁰ But a minority stockholder in a failing corporation cannot complain that the corporate property sold to pay debts was purchased by or in behalf of majority stockholders, where the former was not misled and there was no fraud.⁶¹

§ 4036. — Operation and effect. If a solvent corporation deeds lands to its stockholders without objection from creditors, the beneficial interest passes as well as the legal title.⁶²

§ 4037. Dealings between corporations where one owns majority of stock of another.⁶³

§ 4041. Recovery on implied contract—For personal services. A stockholder may be awarded compensation for services performed by him.⁶⁴ He is entitled to compensation for services rendered in selling corporate property, where the services were rendered on the request of the corporation.⁶⁵

§ 4042. Individual profits. Where a large stockholder is selected as agent to sell corporate property, secret profits made by him, to the detriment of the other stockholders, may be recovered back.⁶⁶ Fraud of a stockholder resulting in another

⁵⁸ See § 4140, *infra*.

⁵⁹ *Alexander v. Dove*, 231 Mass. 362, 121 N. E. 74.

⁶⁰ *Tierney v. United Pocahontas Coal Co.*, — W. Va. —, 102 S. E. 249, citing *Fletcher Cyc. Corp.* § 2360.

⁶¹ *Marcoux v. Reardon*, 203 Mich. 506, 169 N. W. 893.

⁶² See *City of Ft. Worth v. Na-*

tional Park Bank, 261 Fed. 817.

⁶³ See § 4035, *supra*.

⁶⁴ See *Mitchell v. Forest City Printing Co.*, 187 N. Y. App. Div. 743, 176 N. Y. Supp. 157.

⁶⁵ *Hjorth Oil Co. v. Curtis*, 25 Wyo. 1, 3 A. L. R. 765 with note, 163 Pac. 362.

⁶⁶ *Smith v. Smith*, — Tex. Civ. App. —, 213 S. W. 273.

stockholder illegally obtaining secret profits, makes the former equally liable therefor even though he received no part of such profits.⁶⁷ There can be no recovery against stockholders on the ground of alleged secret profits where they, to protect advances made to the corporation, buy in the title to mining claims which the corporation had contracted to purchase with an option to abandon the contract on forfeiture of all payments made, although such stockholders concealed the purchase from the corporation, where the corporation was not injured by the secrecy of the stockholders.⁶⁸

§ 4043. Knowledge of corporate affairs as imputable to stockholders dealing with corporation. A stockholder is not chargeable with notice of the condition of the corporation and of the manner its business was conducted, including a certain sale of stock.⁶⁹ Stockholders are not chargeable with knowledge of the contents of or entries in the ordinary financial books of account of a corporation,⁷⁰ and where a stockholder makes a contract with the corporation, he is not chargeable with constructive notice of a resolution adopted by the board of directors.⁷¹ Notice to certain officers and stockholders is imputed to certain other stockholders whom they represent.⁷²

§ 4044. Purchase of corporate property at forced sale or of claims against the corporation. Where there was a collision between a street car and a train, a stockholder of the street car company had a right to purchase claims of persons injured, even though he intended to benefit the street car company by so doing. This was held in an action by such stockholder, as an assignee of claims, against the steam railway company.⁷³

§ 4046. Stockholders as creditors—Rights as creditor. A stockholder who is also a creditor has the same rights as other creditors,⁷⁴ although it has been held that a stockholder who

⁶⁷ Smith v. Smith, — Tex. Civ. App. —, 213 S. W. 273.

⁶⁸ Munro v. Smith, 243 Fed. 654.

⁶⁹ Murphy v. Estle, 75 Okla. 75, 182 Pac. 83.

⁷⁰ Miley v. Heaney, 168 Wis. 58, 169 N. W. 64.

⁷¹ Cardwell v. Garrison, 176 N. C. 476, 103 S. E. 3.

⁷² Parks v. Hughes, 145 La. 221, 82 So. 202.

⁷³ Ellis v. Chicago & N. W. R. Co., 167 Wis. 392, 167 N. W. 1048.

⁷⁴ La Salle St. Trust & Savings

advanced money to a corporation to pay a mortgage is not subrogated to the rights of the mortgagee.⁷⁵

§ 4048. Dealings with corporate property.⁷⁶ An ex-stockholder may buy the interest of the lessor in a lease in which the corporation is the assignee of the lessee, and enforce the payment of rent, although he was one of several stockholders who obtained the lease and assigned it to the corporation.⁷⁷

XXXI. ACTIONS BY STOCKHOLDERS TO ENFORCE INDIVIDUAL RIGHTS,
OR REDRESS OR PREVENT INDIVIDUAL INJURIES

§ 4050. In general.⁷⁸ Stockholders have no cause of action for the bringing of suits against the corporation, causing incidental injury to the stockholders.⁷⁹ A purchaser of all the rest of the corporate stock, including the good-will of the corporation, may sue as an individual, rather than in a representative capacity, for breach of the contract in regard to good-will.⁸⁰ The bringing of a stockholders' suit does not bar a subsequent action as an individual against corporate officers.⁸¹

In an action by minority stockholders against a majority stockholder to hold the latter as trustee, for the plaintiffs individually, of the proceeds of sales of corporate property, the corporation is not a necessary defendant.⁸²

XXXII. REMEDIES OF STOCKHOLDERS FOR INJURIES TO CORPORATION;
RIGHTS OF ACTION AND PROCEDURE

§ 4051. In general; corporate and individual injuries distinguished. A derivative action by a stockholder is distinguish-

Bank v. Topeka Milling Co., 101 Kan. 446, L. R. A. 1918 A 574, 167 Pac. 1036.

⁷⁵ Karasik v. People's Trust Co., 252 Fed. 324.

⁷⁶ Whether transaction by stockholder a payment or a purchase of a note executed by the corporation, see Kelley v. Briggs, — Mo. App. —, 223 S. W. 959.

⁷⁷ Jarvis v. G. & J. Coal Co., 203 Ill. App. 471.

⁷⁸ See also § 4051, *infra*.

Distinction between representa-

tive action and one brought by stockholders in their own right, see Major v. American Malt & Grain Co., 110 N. Y. Misc. 132, 181 N. Y. Supp. 152.

⁷⁹ Hodge v. Meyer, 252 Fed. 479.

⁸⁰ Komow v. Simplex Cloth-Cutting Mach. Co., 109 N. Y. Misc. 358, 179 N. Y. Supp. 682.

⁸¹ Higgins v. Applebaum, 186 N. Y. App. Div. 682, 174 N. Y. Supp. 807.

⁸² Southern Pac. Co. v. Bogert, 250 U. S. 483, 63 L. Ed. 1099.

able from a direct action as an individual.⁸³ A stockholder cannot sue for the corporation except under certain conditions.⁸⁴ A cause of action belonging to a corporation cannot be asserted by stockholders as individuals, especially where the corporation is not a party.⁸⁵

What is a personal cause of action and what is a representative cause of action is not determinable by the relief sought.⁸⁶ Alleging that wrongful acts of directors are the result of a conspiracy does not change the character of an action by a stockholder from a derivative one to an individual one.⁸⁷ Acts which may result in depreciating the value of corporate stock give a cause of action to a stockholder not individually but merely as a representative of the corporation.⁸⁸ Improper manipulation of funds by the controlling stockholder creates a cause of action in favor of the corporation rather than in favor of a stockholder as an individual.⁸⁹ A cause of action for an accounting from majority stockholders for conspiracy in dissolving a corporation and organizing a new one, involving an alleged wrongful division of assets, is a representative one and not one which can be brought by minority stockholders in their own right.⁹⁰ A suit by a stockholder against bank directors for negligence relating to loans, whereby corporate losses were sustained resulting in an assessment on stockholders, is a derivative one and not an action as an individual.⁹¹ Majority stockholders who enter into a contract to consolidate the corporation have no individual right of action for damages for wrongful interference by third persons causing a breach of the contract, the injury being to the corporation.⁹²

⁸³ *Rothbart v. Star Wet Wash Laundry Co.*, 185 N. Y. App. Div. 807, 174 N. Y. Supp. 76.

⁸⁴ *Zadek v. Merchants' Bank*, — Ala. —, 85 So. 552.

⁸⁵ *Merchants' Bank of Mobile v. Zadek*, — Ala. —, 84 So. 715.

⁸⁶ *Rothbart v. Star Wet Wash Laundry Co.*, 185 N. Y. App. Div. 807, 174 N. Y. Supp. 76.

⁸⁷ *Lukach v. Blair*, 108 N. Y. Misc. 20, 178 N. Y. Supp. 8.

⁸⁸ *Snyder v. Bender*, 173 N. Y. Supp. 401.

⁸⁹ *Baillie v. Columbia Gold Min. Co.*, 86 Ore. 1, 166 Pac. 965.

⁹⁰ *Major v. American Malt & Grain Co.*, 110 N. Y. Misc. 132, 181 N. Y. Supp. 152.

⁹¹ *Harris v. Waters*, 112 N. Y. Misc. 640, 183 N. Y. Supp. 721.

⁹² *Hodge v. Meyer*, 252 Fed. 479.

§ 4052. Right to sue at law. Stockholders cannot sue at law as individuals where the cause of action belongs to the corporation.⁹³

§ 4053. Right to sue in equity or equitable action. Equity has jurisdiction of a stockholders' suit to set aside an issue of stock because absorbed by the directors without giving other stockholders a chance to subscribe thereto, where the control of the corporation is involved, since the remedy at law for damages for an improper sale of stock may be entirely inadequate.⁹⁴ Adequate remedy at law is no defense to an action under section 91a of the New York General Corporation Law providing for a suit in equity by a corporation or its receiver or trustee in bankruptcy to compel one or more directors or officers to account for injuries to or losses of corporate funds through negligence or omission to act.⁹⁵

§ 4054. Statutory remedies and rights of action.⁹⁶

§ 4056. Right as affected by insolvency, receivership or bankruptcy. A stockholders' suit, after dissolution of the corporation, can be brought only after demand on and refusal of the liquidating trustees to sue.⁹⁷ Where the corporation is a bankrupt, stockholders cannot sue on a contract made primarily for the benefit of the corporation and only secondarily or indirectly for the benefit of the stockholders, without first making a demand on the trustee in bankruptcy to sue.⁹⁸

§ 4058. Who are regarded as stockholders entitled to sue—In general. A person entitled to receive, on the distribution of the estate of a decedent, shares of stock, is not a stockholder

⁹³ *Adams v. Haselden*, 112 S. C. 32, 99 S. E. 762.

⁹⁴ *Glenn v. Kittanning Brewing Co.*, 259 Pa. 510, L. R. A. 1918 D 738, Ann. Cas. 1918 D 769, 103 Atl. 340.

⁹⁵ *Woolson Spice Co. v. Columbia Trust Co.*, 193 N. Y. App. Div. 661, 184 N. Y. Supp. 484; *General American Coffee Co. v. Diehl*, 86 N. Y. Misc. 547, 149 N. Y. Supp. 413.

⁹⁶ Actions against officers, see § 2620 et seq., supra; appraisal of stock of dissenting stockholder, see § 4027, supra.

⁹⁷ *Major v. American Malt & Grain Co.*, 110 N. Y. Misc. 132, 181 N. Y. Supp. 152.

⁹⁸ *Horning v. Louis Peters & Co.*, 202 Mich. 140, 167 N. W. 874.

entitled to bring a stockholders' suit.⁹⁹ Where a will bequeathed stock to be held in trust during the life of testator's wife and then to be equally divided as a part of the residuary estate, the residuary legatees take no title to the stock, on the death of the wife, so as to be entitled to bring a stockholders' suit, where the intention was for the executors to sell the stock and divide the proceeds.¹

A stockholder of a holding company may bring a representative action in behalf of a subsidiary company where the directors of both the corporations refuse to sue.²

§ 4060. — Transferees after injury complained of. Subsequent purchasers of stock cannot attack prior legal acts of the corporation, and occupy no better position than any other minority stockholder.³ A stockholder may bring a stockholders' suit, where it is claimed shares of stock were improperly issued to promoters, where the corporation has suffered a tangible wrong or injury, without regard to whether the stockholders suing acquired their stock before or after the wrongful acts complained of, where they are not mere interlopers nor for any reason estopped from suing.⁴ A transferee of stock acquires no better standing to attack acts of officers as negligent than the transferor would have had if he had continued to own the stock.⁵

§ 4061. Grounds and occasions for relief—In general. Dissenting minority stockholders may sue to set aside a sale of corporate property for an inadequate consideration, where the board of directors refuse to act.⁶

⁹⁹ *Whitaker v. Whitaker Iron Co.*, 249 Fed. 531, aff'g 238 Fed. 980.

¹ *Whitaker v. Whitaker Iron Co.*, 249 Fed. 531.

² A stockholder in a holding company may in some circumstances maintain a representative action for the benefit of the subsidiary company and thus indirectly for the advantage of the holding company. *Holmes v.*

Camp, 180 N. Y. App. Div. 409, 167 N. Y. Supp. 840, where question was said to be one never decided before.

³ *Bernheim v. Wallace*, 186 Ky. 459, 217 S. W. 916.

⁴ *Roberson v. Draney*, — Utah —, 178 Pac. 35.

⁵ *Harris v. Rogers*, 190 N. Y. App. Div. 208, 179 N. Y. Supp. 799.

⁶ *Bentley v. Zelma Oil Co.*, 76 Okla. 116, 184 Pac. 131.

§ 4062. — **Ultra vires acts, waste, diversion or misapplication of assets.** Fraud not only substantially injuring the rights of minority stockholders, but also tending to destroy such rights, warrants a stockholders' suit.⁷ A stockholders' suit lies in case of fraudulent appropriation of corporate funds and the destruction of the corporate property through the agency of the directors.⁸ Minority stockholders may sue to cancel conveyances of corporate property fraudulently made by corporate officers,⁹ or to cancel stock wrongfully issued without consideration.¹⁰

§ 4064. — **Wrongdoing or neglect by officers and directors.** Fraud of officers is ground for a stockholders' suit.¹¹ A stockholder may sue in behalf of the corporation to enforce the liability of directors for fraud, mismanagement, etc.¹²

§ 4065. — **Impolitic and inexpedient acts and dealings; discretion in management and policy.** Courts cannot interfere in matters relating to internal management of the corporation.¹³ Whether an act is good business is exclusively a question for the board of directors.¹⁴ Courts will not substitute their judg-

⁷ *Bates v. Werries*, 198 Mo. App. 209, 199 S. W. 758.

⁸ *James v. P. B. Steifer Min. Co.*, 35 Cal. App. 778, 171 Pac. 117.

⁹ *Bentley v. Zelma Oil Co.*, 75 Okla. 116, 184 Pac. 131.

¹⁰ A stockholders' suit lies to cancel stock issued by directors in exchange for worthless land. *James v. P. B. Steifer Min. Co.*, 35 Cal. App. 778, 171 Pac. 117.

¹¹ *James v. P. B. Steifer Min. Co.*, 35 Cal. App. 778, 171 Pac. 117; *Steitz v. Old Dominion Copper Mining & Smelting Co.*, 89 N. J. Eq. 265, 104 Atl. 214.

¹² *Smith v. Rader*, 31 Idaho 423, 173 Pac. 970, and see § 2679 et seq., supra.

¹³ *Du Pont v. Du Pont*, 256 Fed. 129, aff'g 251 Fed. 937; *Haldeman v. Haldeman*, 176 Ky. 635, 197 S. W. 376; *People ex rel. Western*

U. Tel. Co. v. Public Service Commission, 192 N. Y. App. Div. 748, 183 N. Y. Supp. 659; *Thurmond v. Paragon Colliery Co.*, 82 W. Va. 49, 95 S. E. 816. See *Cuppy v. Ward*, 187 N. Y. App. Div. 625, 176 N. Y. Supp. 233.

Internal affairs of a religious corporation cannot be interfered with by the courts. *King v. Smith*, 106 Kan. 624, 189 Pac. 147.

The discretion of the directors to raise money to pay debts by a sale of a part or all of the unissued stock, instead of by other means, will not be interfered with by the courts, since relating to internal management. *Thurmond v. Paragon Colliery Co.*, 82 W. Va. 49, 95 S. E. 816.

¹⁴ *General Inv. Co. v. Bethlehem Steel Corporation*, 248 Fed. 303, 312.

ment for that of the governing body of the corporation, at the instances of minority stockholders, unless the acts complained of are so clearly against the interest of the minority as to amount to a wanton and fraudulent destruction of their rights and constitute a clear, substantial and flagrant violation of corporate duty.¹⁵

For instance, a court of equity cannot substitute its judgment for that of the corporation, acting through its directors or stockholders, as to whether the corporation should acquire an asset to which it has no title but merely an inchoate right to assert a title.¹⁶ In a stockholders' suit against a director in behalf of the corporation, alleged excessive salary paid to him as president, manager, etc., cannot be recovered, where the corporation has refused to sue, unless the corporation has acted in bad faith or fraudulently.¹⁷

§ 4068. Prerequisites and conditions to suit by stockholder—Demand on, and refusal by corporation to sue.¹⁸ Where stockholders sue as representing the corporation, it is a condition precedent that they first seek relief through the corporation where there is no legal excuse for not doing so.¹⁹ In some jurisdictions, however, this rule as to demand, etc., does not apply to a suit against the corporation by a stockholder, seeking, in his own direct right, to enjoin it from doing an illegal act.²⁰

§ 4070. — Facts dispensing with demand and the like. No demand is necessary where it would be a mere useless form.²¹

¹⁵ *Rice v. Thomas*, 184 Ky. 168, 211 S. W. 428.

¹⁶ *Du Pont v. Du Pont*, 246 Fed. 332.

Whether a corporation shall take over a purchase of its stock by one of its officers, is a matter of corporate policy with which the courts will not ordinarily interfere. *Du Pont v. Du Pont*, 256 Fed. 129, aff'g on this point 251 Fed. 937.

¹⁷ *Lane v. Wood*, — Vt. —, 106 Atl. 656.

¹⁸ See also § 4056, supra.

¹⁹ *Soghomonian v. Garabedian*, 231 Mass. 445, 121 N. E. 401; *Soloway v. Junius Coal & Wood Co.*, 186 N. Y. App. Div. 879, 175 N. Y. Supp. 1; *Passmore v. Allentown & Reading Traction Co.*, — Pa. —, 110 Atl. 240; *Barthold v. Thomas*, — Tex. —, 210 S. W. 506; *Moore v. Lewisburg & R. E. R. Co.*, 80 W. Va. 653, L. R. A. 1918 A 1028, 93 S. E. 762.

²⁰ *General Inv. Co. v. Lake Shore & M. S. Ry. Co.*, 250 Fed. 160, 174, aff'g 226 Fed. 976.

²¹ *James v. P. B. Steifer Min.*

For instance, where the alleged wrongdoing is that of a majority of the directors, no demand is necessary.²² A stockholder may sue without requesting the corporation to sue where the corporation is under the control of directors who are liable for the loss sought to be recovered.²³

The mere fact that directors were elected by the vote of the guilty stockholder is no excuse for failure to make a demand on the directors.²⁴

§ 4071. Defenses and objections to suit—In general. Where a corporation refuses to sue directors for secret profits, a minority stockholder cannot sue where his conduct has been that of one trying to sue only when the directors refused to give him a part of such profits.²⁵ Assignments and releases by stockholders are no defense to a stockholders' suit against directors, it being a derivative action.²⁶ A stockholder's suit to set aside a sale of all the corporate property, because of defects relating to the meeting of the directors and inadequacy of price, is not barred by the pendency of an action brought by the corporation to enforce the sale.²⁷

§ 4072. — Laches, estoppel, ratification or compromise—In general. Laches bars a stockholders' suit,²⁸ but there is no

Co., 35 Cal. App. 778, 171 Pac. 117; *Gordon v. Brucker*, 208 Ill. App. 188; *Tasler v. Peerless Tire Co.*, 144 Minn. 150, 174 N. W. 731; *Liggett v. Roanoke Water Co.*, — Va. —, 101 S. E. 55.

²² *Magale v. Fomby*, 132 Ark. 289, 201 S. W. 278; *Smith v. Rader*, 31 Idaho 423, 173 Pac. 970; *Almy v. Almy, Bigelow & Washburn, Inc.*, — Mass. —, 126 N. E. 419; *Snyder v. Bender*, 173 N. Y. Supp. 401; *Glenn v. Kittanning Brewing Co.*, 259 Pa. 510, L. R. A. 1918 D 738, Ann. Cas. 1918 D 769, 103 Atl. 340; *Moore v. Lewisburg & R. E. R. Co.*, 80 W. Va. 653, L. R. A. 1918 A 1028, 93 S. E. 762.

²³ *Proctor v. Farrar*, — Mo. —, 213 S. W. 469.

²⁴ *Baillie v. Columbia Gold Min. Co.*, 86 Ore. 1, 166 Pac. 965.

²⁵ *Fullerton v. Crawford*, 50 Dom. L. Rep. (Can.) 457.

²⁶ *Harris v. Waters*, 112 N. Y. Misc. 640, 183 N. Y. Supp. 721.

²⁷ *Glidden v. Diamond 66 Cattle & Dairy Co.*, 178 Cal. 562, 174 Pac. 667.

²⁸ *Woodward v. Huron Implement Co.*, 200 Mich. 523, 166 N. W. 1025; *Carrier v. Dixon*, 142 Tenn. 122, 218 S. W. 395. See *Williams v. Croft Hat & Notion Co.*, 82 W. Va. 549, 96 S. E. 929.

Six months' delay held not laches in *Almy v. Almy, Bigelow & Washburn, Inc.*, — Mass. —, 126 N. E. 419.

Delay of twelve years in seeking redress for fraud, where un-

laches until the facts are known or should have been discovered.²⁹

It has been held that the defense of laches or statute of limitations cannot be urged by the corporation in a stockholders' suit but only by the individual defendants alleged to be wrongdoers.³⁰

§ 4076. — Limitation of action. The cause of action does not accrue, within the statute of limitations, until the discovery of the fraud.³¹ In California, a stockholders' suit to set aside a fraudulent issue of securities to promoters may be brought within three years from the discovery of the facts constituting the fraud or of facts putting a prudent man on inquiry.³²

Minority of the plaintiff stockholder does not toll the statute of limitations where he sues not as an individual but as representing the corporation.³³

§ 4077. — Bad motive or want of substantial interest.³⁴

§ 4079. Jurisdiction of action or suit.³⁵ A stockholders' suit, where officers have misappropriated assets, may be brought against a foreign corporation, where officers have transacted the corporate business in the state.³⁶

In a stockholders' suit in a federal court, where the officers or persons controlling the corporation are opposed to the object sought by the complaining stockholders, the corporation will be aligned with the defendants as to diversity of citizenship.³⁷

explained, bars a stockholders' suit by minority stockholders. *Whitaker v. Whitaker Iron Co.*, 249 Fed. 531.

²⁹ *Williams v. Croft Hat & Notion Co.*, 82 W. Va. 549, 96 S. E. 929.

³⁰ *Baillie v. Columbia Gold Min. Co.*, 86 Ore. 1, 167 Pac. 1167.

³¹ *James v. P. B. Steifer Min. Co.*, 35 Cal. App. 778, 171 Pac. 117.

³² *Beal v. Smith*, — Cal. App. —, 189 Pac. 341.

³³ *Magale v. Fomby*, 132 Ark. 289, 201 S. W. 278.

³⁴ See § 3982, *supra*.

³⁵ Venue of action by stockholder to set aside resolution as fraudulent and a conveyance of real estate pursuant thereto, see *Dial v. Homestead Land & Building Co.*, 39 Cal. App. 479, 179 Pac. 444.

³⁶ *Tasler v. Peerless Tire Co.*, 144 Minn. 150, 174 N. W. 731.

³⁷ *Whitaker v. Whitaker Iron Co.*, 238 Fed. 980, and see § 2967, *supra*.

§ 4080. Parties plaintiff. In an action by minority stockholders against majority stockholders, brought on behalf of all the stockholders, other minority stockholders should be permitted to intervene.³⁸ The fact that other minority stockholders do not join in a suit by a minority stockholder based on alleged fraud of the majority stockholders is worthy of consideration.³⁹ A person is no less a creditor entitled to intervene in a stockholders' suit because the time for the payment to him of his debt has not matured.⁴⁰ Stockholders of a holding company may join with stockholders of a subsidiary company in a stockholders' suit for the benefit of the subsidiary company.⁴¹ A pledgee of stock may join in a stockholders' suit.⁴² Minority directors, the same as minority stockholders, may sue, under equity rule 27 of the federal courts.⁴³

§ 4081. Parties defendant—The corporation, officers and other stockholders. Generally the corporation is a necessary party defendant,⁴⁴ at least where the suit is against directors for fraud, mismanagement, etc.⁴⁵ In an action by minority stockholders to enjoin a corporate act in fraud of their rights, majority stockholders at whose instance such act was to be done need not be joined as defendants.⁴⁶ Liquidating trustees are necessary parties to a stockholders' suit.⁴⁷

In federal courts, under the new equity rules, where minority stockholders sue in behalf of the corporation, alleging transactions by directors defrauding the corporation of property for their personal benefit, where a resident director is made a defendant, other directors out of the jurisdiction and who can-

³⁸ *Southern Pac. Co. v. Bogert*, 250 U. S. 483, 63 L. Ed. 1099, modifying 244 Fed. 61.

³⁹ *Presidio Min. Co. v. Overton*, 261 Fed. 933.

⁴⁰ *Morse v. Metropolitan S. S. Co.*, 88 N. J. Eq. 235, 102 Atl. 524.

⁴¹ *Holmes v. Camp*, 180 N. Y. App. Div. 409, 167 N. Y. Supp. 840.

⁴² *Boyd v. Applewhite*, — Miss. —, 84 So. 16.

⁴³ *Curtis v. Metcalf*, 259 Fed. 961.

⁴⁴ *McNeely v. E. I. Du Pont de Nemours Powder Co.*, 263 Fed. 252; *Barthold v. Thomas*, — Tex. —, 210 S. W. 506.

⁴⁵ *Smith v. Rader*, 31 Idaho 423, 173 Pac. 970.

⁴⁶ *Southwestern Portland Cement Co. v. Latta & Happer*, — Tex. Civ. App. —, 193 S. W. 1115.

⁴⁷ *Major v. American Malt & Grain Co.*, 110 N. Y. Misc. 132, 181 N. Y. Supp. 152.

not be served and whose joinder would oust the jurisdiction of the court, are not necessary defendants.⁴⁸

§ 4082. — Third persons or corporations involved in controversy. A stockholders' suit for rescission or accounting for profits, alleging transfer of corporate property in satisfaction of judgment and subsequent transfers, need not make the ultimate transferee a defendant.⁴⁹ In a stockholders' suit to annul a contract between their corporation and another, a third corporation which was sought to be enjoined from disposing of the stock of the corporation in which complainants are stockholders is not a necessary party.⁵⁰

§ 4083. Pleading and procedure—In general. The bill must not be multifarious.⁵¹ A bill by stockholders to redress both corporate and individual wrongs is multifarious,⁵² and even in code states a stockholder cannot join in one action a personal cause of action and a cause of action as a representative of the corporation.⁵³ In a stockholders' suit in behalf of the corporation, although the corporation is made a defendant, the stockholders cannot join causes of action that the corporation could not have joined.⁵⁴

§ 4084. — Alleging cause of action and plaintiff's right as stockholder.⁵⁵ If the complaint states that plaintiff is a di-

⁴⁸ Krouse v. Brevard Tannin Co., 249 Fed. 538.

⁴⁹ Steitz v. Old Dominion Copper Mining & Smelting Co., 89 N. J. Eq. 265, 104 Atl. 214.

⁵⁰ Subers v. Continental Securities Co., — Del. Ch. —, 111 Atl. 433.

⁵¹ See Almy v. Almy, Bigelow & Washburn, Inc., — Mass. —, 126 N. E. 419.

Joinder of causes of action, see Snyder v. Bender, 173 N. Y. Supp. 401.

⁵² Zadek v. Merchants' Bank, — Ala. —, 85 So. 552.

⁵³ Monte Rico Mining & Min-

eral Co. v. Fleming, 258 Fed. 106; Beal v. United Properties Co., — Cal. App. —, 189 Pac. 346; James v. P. B. Steifer Min. Co., 35 Cal. App. 778, 171 Pac. 117.

⁵⁴ Blake v. Boston Development Co., 50 Utah 347, 167 Pac. 672.

⁵⁵ Form of petition in stockholders' suit is set forth in Proctor v. Farrar, — Mo. —, 213 S. W. 469; Shaw v. Sanitary Street Flushing Mach. Co., — Mo. —, 213 S. W. 83.

Complaint as alleging cause of action in favor of stockholder as representative of corporation, see

rector, it need not state in the title of the action the representative capacity in which he sues, in an action under sections 90 and 91 of the General Corporation Law of New York to compel directors and officers to account for corporate property converted to their own use.⁵⁶

§ 4085. — Allegations as to demand and refusal of corporation to sue. The complaint in a stockholders' suit must state a demand on the corporation to sue or else an excuse therefor.⁵⁷ A general statement that the corporation or its board of directors is in control of the guilty party is not sufficient.⁵⁸ In a stockholders' suit, plaintiff may plead not only a demand on the corporation to sue and its refusal but also that the defendants who have acted fraudulently are in control of the corporation.⁵⁹

§ 4086. — Allegations under 94th Equity Rule (New Equity Rule 27) in federal courts. Under rule 27 of the federal equity rules, a stockholders' bill in a federal court must contain a verified allegation that the suit is not a collusive one to confer jurisdiction on the federal court in a case which it otherwise would not have cognizance of.⁶⁰ The bill in a stockholders' suit, in a federal court, is sufficient, unless a motion is made for further and better particulars, where it alleges that the transactions complained of were brought to the attention of the directors, although not stating the time, place, etc., and where the date when complainants became stockholders was not stated.⁶¹

§ 4089. Conduct and control of action; discontinuances and compromises. Plaintiff in a stockholders' suit may dismiss it, although brought in favor of a class.⁶² Where one minority

Rothbart v. Star Wet Wash Laundry Co., 185 N. Y. App. Div. 807, 174 N. Y. Supp. 76.

⁵⁶ Higgins v. Applebaum, 183 N. Y. App. Div. 527, 170 N. Y. Supp. 228.

⁵⁷ Glidden v. Diamond 66 Cattle & Dairy Co., 178 Cal. 562, 174 Pac. 667.

⁵⁸ Baillie v. Columbia Gold Min.

Co., 86 Ore. 1, 166 Pac. 965.

⁵⁹ MacLean v. J. L. Mott Iron Works, 193 N. Y. App. Div. 698, 184 N. Y. Supp. 332.

⁶⁰ Laughner v. Schell, 260 Fed. 396.

⁶¹ Krouse v. Brevard Tannin Co., 249 Fed. 538.

⁶² Bernheim v. Wallace, 186 Kv. 459, 217 S. W. 916.

stockholder sues for the use and benefit of several other stockholders, he should not be allowed to enter any order or make any settlement prejudicial to the interests of the other minority stockholders, but he may make a settlement fully protecting the rights of such other stockholders.⁶³

§ 4090. Judgment and nature of relief allowable—In general. A money judgment against a director may be rendered in a stockholders' suit.⁶⁴ In such a suit the court should protect minority stockholders not parties of record, by preventing any orders or judgment or settlement prejudicial to their interests.⁶⁵

§ 4091. — Injunction, receivership and accounting; dissolution. A temporary injunction is often proper to prevent acts of the officers pending suit.⁶⁶ In a stockholders' suit, a decree enjoining the solvent company from transacting any corporate business and also enjoining certain stockholders from disposing of their stock, is too broad.⁶⁷

§ 4092. — Bar and conclusiveness of decree. The judgment is conclusive not only upon the stockholders who brought the suit but upon the corporation also and upon those who had the right to intervene but did not avail themselves of it.⁶⁸

§ 4093. — Costs and fees and allowances. In a stockholders' suit, costs are properly awarded against the corporate officer whose misconduct rendered the litigation necessary.⁶⁹ An attorney's fee cannot be recorded as a part of the costs in a stockholders' suit where not expressly authorized by statute.⁷⁰ In stockholders' suits, other minority stockholders joined as plaintiffs by order of court, who have rendered valuable services

⁶³ *Bernheim v. Wallace*, 186 Ky. 459, 217 S. W. 916.

⁶⁴ *Boulicault v. Oriel Glass Co.*, — Mo. —, 223 S. W. 423.

⁶⁵ *Bernheim v. Wallace*, 186 Ky. 459, 217 S. W. 916.

⁶⁶ *Monte Rico Mining & Mineral Co. v. Fleming*, 258 Fed. 106.

⁶⁷ *Monte Rico Mining & Mineral Co. v. Fleming*, 258 Fed. 106.

⁶⁸ *Dana v. Morgan*, 232 Fed. 85.

⁶⁹ *South Norfolk Land Co. v. Tebault*, — Va. —, 98 S. E. 679.

⁷⁰ *McArthur v. John McArthur Co.*, 39 Cal. App. 704, 179 Pac. 700.

Attorney's fees cannot be awarded against the corporation in a stockholders' suit although the stockholders are successful. See *Roberson v. Draney*, — Utah —, 178 Pac. 35.

are entitled to compensation out of the fund, as well as the original plaintiff.⁷¹ Where a minority stockholder, by suing, prevents officers from carrying out a fraudulent scheme and sacrificing the corporate assets, he may thereafter bring a separate suit for reimbursement for attorney's fees in the first action as well as other expenses to the extent of the value of the assets saved to the company.⁷²

XXXIII. LIABILITY OF STOCKHOLDERS TO CREDITORS ON ACCOUNT OF UNPAID SUBSCRIPTIONS

§ 4098. Existence of liability—Conflict of laws. The obligation of stockholders to creditors for balances on their stock is to be determined by the law of the state where the corporation was created.⁷³

§ 4099. Nature and extent of liability—Nature of liability. The liability of subscribers to creditors on unpaid stock is several and not joint.⁷⁴ Where creditors sue stockholders for unpaid stock subscriptions, each stockholder sued is liable in full and not merely for his proportion of the debt.⁷⁵

§ 4100. — Extent of liability in general. It has been held that a trustee in bankruptcy suing for balances due on stock need not show that the assets are insufficient to pay creditors.⁷⁶ Where the stockholder agrees to pay more than par, he is liable to creditors for the balance due on the contract price and not on the par value of the stock.⁷⁷ A court or jury cannot fix

⁷¹ *Goodwin v. Milwaukee Lithographing Co.*, — Wis. —, 177 N. W. 618.

⁷² *Beyer v. North American Coal & Mining Co.*, — N. D. —, 175 N. W. 216.

⁷³ *McCarty v. More*, — Cal. —, 186 Pac. 140.

⁷⁴ *In re Phoenix Hardware Co.*, 249 Fed. 410, and see § 4127, *infra*.

⁷⁵ *Olson Mfg. Co. v. Rex Motor Co.*, 203 Mich. 470, 170 N. W. 64.

⁷⁶ *Benner v. Billings*, 107 Wash. 1, 181 Pac. 19.

⁷⁷ *Levassor v. Metropolitan*

Fire Ins. Co.'s Receiver, 188 Ky. 23, 220 S. W. 752.

Where the par value of preferred stock was \$25 a share and subscribers paid \$35 a share with common stock thrown in as a bonus, common stockholders sued by creditors for the amount due on their common stock are not entitled to a credit for the premium paid on the preferred stock. *Stoecker v. Goodman*, 183 Ky. 330, 209 S. W. 374.

In an earlier case it was held that if subscriptions are made

“the amount that is unpaid upon the stock,” as required by the South Dakota statute making stockholders liable to creditors for such amount, where mining property was exchanged for stock and there is no evidence to fix such amount.⁷⁸

§ 4101. — Liability for interest and costs. Expenses and compensation of a receiver are taxable as costs against stockholders in a proceeding to collect from them the balance due on unpaid stock.⁷⁹ In proceedings by a receiver of an insolvent company to enforce liability for unpaid stock, interest on creditor's claims should commence to run at the time the receivers asked the court to make the assessment.⁸⁰ Stockholders are liable for the costs and expenses of administering the estate, including counsel fees and the compensation of the receiver, not only for services rendered in protecting the estate but also for services rendered in suits against stockholders to collect assessments.⁸¹

§ 4103. Defenses available to stockholders—In general.⁸² Holders of preferred stock cannot escape liability for unpaid subscriptions on the ground that the stock was void because the common stock had not been paid for in cash to the company.⁸³ Even if an agreement that the stock is not to be paid for may be considered void as in violation of constitutional or statutory provisions, the subscription makes the stockholder liable to creditors for the amount unpaid.⁸⁴ Common stockholders are liable for unpaid subscriptions although subscriptions to the preferred stock have not first been collected.⁸⁵ The assignment of the

above par, subscribers cannot reduce recovery by the receiver to the amount of the par value of the stock. *Preston v. Jeffers*, 179 Ky. 384, 200 S. W. 654.

⁷⁸ *Clinton Mining & Mineral Co. v. Jamison*, 256 Fed. 577, 582.

⁷⁹ *Du Pont v. Ball*, 11 Del. Ch. 430, 106 Atl. 39, modifying *John W. Cooney Co. v. Arlington Hotel Co.*, 11 Del. Ch. 286, 101 Atl. 879.

⁸⁰ *Du Pont v. Ball*, 11 Del. Ch. 430, 106 Atl. 39, modifying *John W. Cooney Co. v. Arlington Hotel*

Co., 11 Del. Ch. 286, 101 Atl. 879.

⁸¹ *Levassor v. Metropolitan Fire Ins. Co.'s Receiver*, 188 Ky. 23, 220 S. W. 752, citing *Fletcher Cyc. Corp.* § 4101.

⁸² See, as to watered stock, §§ 3586, 3587, 3595.

⁸³ *Du Pont v. Ball*, 11 Del. Ch. 430, 106 Atl. 39, modifying *John W. Cooney Co. v. Arlington Hotel Co.*, 11 Del. Ch. 286, 101 Atl. 879.

⁸⁴ *Jensen v. Aikman*, 32 Idaho 261, 181 Pac. 525.

⁸⁵ *Du Pont v. Ball*, 11 Del. Ch.

judgment to certain stockholders, pending an action by the judgment creditor against stockholders who had paid nothing on their stock, does not preclude the prosecution of the action against other stockholders.⁸⁶ A subscriber cannot escape liability on his subscription, in an action by the receiver, on the ground that he signed merely for the purpose of incorporating, since the receiver represents creditors as well as stockholders.⁸⁷

The receiver may sue to collect unpaid stock subscriptions although the creditors had no knowledge of such failure to pay when their debts were created.⁸⁸ But creditors with knowledge of the insufficiency of the consideration for the issuance of paid up stock cannot recover.⁸⁹

§ 4104. — Release or discharge of stockholders. Payment of a stock subscription by a third person bars an action for an unpaid balance.⁹⁰ Where a subscription is with the option of rescinding, and rescission is made before the company is organized or any liabilities incurred by it, the subscriber is not liable, as a stockholder, to subsequent creditors.⁹¹ Liability as a stockholder to creditors on unpaid stock does not exist after the stockholder has surrendered his stock in consideration of a reconveyance of the property originally turned in by him as payment for the stock.⁹² But liability to creditors for unpaid balances cannot be defeated by rescission of the subscription as per contract after the commencement of the action nor where the right to rescind had been waived.⁹³

Without consideration, directors cannot release subscriptions to stock; but a dispute as to an unpaid subscription may be compromised by the directors, where the corporation is solvent.⁹⁴

430, 106 Atl. 39, modifying *John W. Cooney Co. v. Arlington Hotel Co.*, 11 Del. Ch. 286, 101 Atl. 879.

⁸⁶ *Scott v. Luehrmann*, 278 Mo. 638, 213 S. W. 855.

⁸⁷ *Schmitt v. Kulamer*, — Pa. —, 110 Atl. 169.

⁸⁸ *Mitchell v. Porter*, — Tex. Civ. App. —, 194 S. W. 981.

⁸⁹ See § 3595, *supra*.

⁹⁰ *Central Trust Co. v. Crawford*, 201 Ill. App. 555.

⁹¹ *Donoho v. Carwile*, — Tex. Civ. App. —, 214 S. W. 553.

⁹² *Donoho v. Carwile*, — Tex. Civ. App. —, 214 S. W. 553.

⁹³ *Barnard v. McIntire*, — Cal. App. —, 187 Pac. 440.

⁹⁴ *Martin v. Cushwa*, — W. Va. —, 104 S. E. 97, citing *Fletcher Cyc. Corp.* § 4104; and see § 639, *supra*.

§ 4105. — **Waiver or release of liability by creditors.** Creditors are not estopped to sue stockholders on unpaid subscriptions, by electing to take over the business, where no injury resulted therefrom and the stockholders acquiesced therein.⁹⁵

§ 4106. — **Estoppel or waiver of right to set up defenses.**⁹⁶ Subscribers to stock are not estopped, as against creditors, to set up the defense of the illegality of the corporation when sued on their subscriptions.⁹⁷ Subscribers to stock, although estopped from urging the defense that the requisite amount of capital stock had never been subscribed, as against third persons who extended credit on the faith of the corporation being duly organized, are not estopped as against the directors who were charged with notice of the deficiency in subscriptions to the stock at the time they extended credit to the corporation.⁹⁸

§ 4107. **Persons liable—In general.** The manner by which a holder of stock acquired title is immaterial, so far as his liability to creditors for an unpaid balance is concerned.⁹⁹ The liability is not affected by whether the holders of the stock were subscribers or whether the stock was issued without subscriptions.¹ An acceptance of certificates of stock makes the acceptor liable thereon, if liable at all, as though he had originally subscribed for it.² One may be the owner of stock, so as to be liable to creditors, where entitled thereto but not actually received.³

One who subscribed for stock on a condition never fulfilled, and who never received stock, is not liable where not even a de facto stockholder.⁴ Where certificates for the whole capital stock have already been issued, a subscriber to stock cannot be held liable to creditors as a stockholder.⁵

⁹⁵ *Hodde v. Hahn*, — Mo. —, 222 S. W. 799.

⁹⁶ See also § 3488, *supra*.

⁹⁷ *Davis v. Allison*, 109 Tex. 440, 211 S. W. 980.

⁹⁸ *Lowe v. Byrd*, — Ga. —, 96 S. E. 1001, which was an action by a trustee in bankruptcy to recover unpaid subscription.

⁹⁹ *Shugart v. Maytag*, — Iowa —, 176 N. W. 886.

¹ *In re Phoenix Hardware Co.*, 249 Fed. 410.

² *Rice v. Thomas*, — Ky. —, 211 S. W. 428.

³ *Rasor v. West Coast Development Co.*, — Ore. —, 192 Pac. 631.

⁴ *Seubert v. Scott*, 39 S. D. 278, 164 N. W. 75.

⁵ *Baldwin v. Timber Inv. Co.*, — N. D. —, 176 N. W. 662.

§ 4111. — Effect of transfer of stock.⁶ Transferees of stock are liable to corporate creditors for unpaid subscriptions the same as transferrers.⁷ The transferrer of stock is not liable to creditors for unpaid subscriptions, unless the transfer was fraudulent; and hence ownership of the stock must be shown as of the time of the commencement of the action to recover unpaid subscriptions.⁸ But stockholders cannot relieve themselves from liability to creditors for unpaid balances by transferring their stock, but not on the corporate books, after demand on them by the creditors for payment.⁹ So where no corporate books were used to record stock transfers, a transferrer of stock is liable for the balance due on the stock where the corporation never consented to the transfer and did not issue a new certificate.¹⁰ A subscriber to stock cannot escape liability for the balance due on the stock, after transferring it, by merely delivering the assignment to an officer of the company or to the attorney for the real incorporators.¹¹

Purchasers of stock from stockholders are liable for corporate debts to the extent the stock is not paid up, under the South Dakota statutes making "each stockholder" liable.¹²

Surrender of stock for cancellation does not terminate liability to creditors for the amount unpaid on the stock, where the stock remains in his name on the corporate books.¹³

§ 4113. By whom liability may be enforced—In general. A creditor is not estopped to enforce stockholders' liability for unpaid subscriptions because he extended credit on faith of his representations as to the results to be obtained from the prop-

⁶For note on "effect of transfer of shares of stock on liability for unpaid subscriptions," see L. R. A. 1918 D 1049.

⁷Zierath v. Claggett, — Cal. App. —, 188 Pac. 837.

A holder of stock with notice is subject to assessment, if the stock is unpaid, although he is not an original subscriber. Sweet v. Barnard, — Colo. —, 182 Pac. 22.

⁸Wilkinson v. Grant, — Cal. App. —, 189 Pac. 319. But see Hodde v. Hahn, — Mo. —, 222

S. W. 799, holding that sale of stock does not relieve the sellers of liability to creditors for balances due on the stock.

⁹Shugart v. Maytag, — Iowa —, 176 N. W. 886.

¹⁰Schmitt v. Kulamer, — Pa. —, 110 Atl. 169.

¹¹Schmitt v. Kulamer, — Pa. —, 110 Atl. 169.

¹²Shugart v. Maytag, — Iowa —, 176 N. W. 886.

¹³McCarty v. More, — Cal. —, 186 Pac. 140.

erty sold, where he had no knowledge that the stock subscribed was not paid in full.¹⁴

§ 4114. — Creditors who are also stockholders. A stockholder who has paid his subscription in full cannot, on insolvency of the corporation, sue as an individual other stockholders for the balance due on their subscriptions.¹⁵

§ 4115. — Receivers, trustees in bankruptcy, assignees for creditors, and the like. A receiver of the corporation may sue to enforce the amount remaining unpaid on subscriptions to stock.¹⁶ So a trustee in bankruptcy may and should collect unpaid stock subscriptions.¹⁷

Where the receiver and the creditors represented by him are in no better position to enforce unpaid subscriptions than the corporation itself, the receiver cannot enforce unpaid subscriptions where the stock was worthless.¹⁸ Even if a corporation because of its agreement, cannot enforce liability on unpaid subscriptions, a receiver appointed under the insolvency statute has the right under the direction of the chancellor to collect such subscriptions.¹⁹

§ 4116. — Limitations on rights of receivers, assignees or trustees.²⁰

§ 4118. Calls and assessments—Necessity for call or assessment; by whom made. Balances due upon unpaid capital stock do not become due until there has been a call or assessment.²¹

¹⁴ Zierath v. Claggett, — Cal. App. —, 188 Pac. 837.

¹⁵ Lumpp v. Drumheller, — Wash. —, 188 Pac. 913, and see § 4211, *infra*.

¹⁶ Hodde v. Hahn, — Mo. —, 222 S. W. 799.

¹⁷ Mills v. Friedman, 111 N. Y. Misc. 253, 181 N. Y. Supp. 285; DeMuth v. Faw, 103 Wash. 379, 174 Pac. 18.

The bankruptcy court has no jurisdiction of an action by the trustee to enforce unpaid subscriptions in a single suit, where

the debts are unconditionally due by the terms of the subscription contract. Kelley v. Gill, 245 U. S. 116, 62 L. Ed. 185, *aff'g* 238 Fed. 996.

¹⁸ Mitchell v. Porter, — Tex. Civ. App. —, 194 S. W. 981.

¹⁹ Du Pont v. Ball, 11 Del. Ch. 430, 106 Atl. 39, modifying John W. Cooney Co. v. Arlington Hotel Co., 11 Del. Ch. 286, 101 Atl. 879.

²⁰ In case of watered stock, see § 3589 *et seq.*, *supra*.

²¹ In re Phoenix Hardware Co., 249 Fed. 410, and see § 4134, *infra*.

Where a corporation is bankrupt direct proceedings to assess the stock are necessary before the liability of a stockholder can be enforced, unless he consents to the absence of such assessment.²² A creditor whose execution against the corporation is returned unsatisfied need not demand the levy of an assessment by the directors to pay his debt before suing stockholders for balances due on their stock.²³

§ 4119. — Procedure to procure assessment. An action to make an assessment for the benefit of creditors, upon holders of unpaid stock in a foreign corporation, cannot be maintained in another state but only in the domicile of the corporation.²⁴ A receiver pendente lite is deemed authorized to file a petition for the assessment of stockholders, where the assessment was ordered, since the order will be deemed as in effect authority to file the petition.²⁵ The return unsatisfied of an execution issued on a judgment against a corporation is a sufficient showing of insolvency to warrant the court in assessing stockholders, although there has been no judicial determination of insolvency.²⁶ The doctrine of laches does not apply to statutory proceedings by a receiver to levy an assessment on the stockholders where the statute of limitations has not extinguished the right to proceed against the stockholders.²⁷ In order to make an assessment on stockholders for the payment of debts of a bankrupt company, the referee must find that the assets are insufficient to pay debts, that all or part of the stock is not paid for in full, and the pro rata share the holders of unpaid stock must pay to liquidate the corporate indebtedness and the expenses of the proceeding.²⁸

§ 4120. — Conclusiveness of call or assessment. The order of a federal court authorizing the trustee of a bankrupt company

²² *In re Manufacturers' Box & Lumber Co.*, 251 Fed. 957.

²³ *McCarty v. More*, — Cal. —, 186 Pac. 140.

²⁴ *McDermott v. Woodhouse*, 87 N. J. Eq. 615, 101 Atl. 375, followed in *Chicago Title & Trust Co. v. Young's Ex'rs*, 90 N. J. Eq. 27, 105 Atl. 601.

²⁵ *Greenfield v. Hill City Land*,

Loan & Lumber Co., 141 Minn. 393, 170 N. W. 343.

²⁶ *Greenfield v. Hill City Land*, *Loan & Lumber Co.*, 141 Minn. 393, 170 N. W. 343.

²⁷ *Greenfield v. Hill City Land*, *Loan & Lumber Co.*, 141 Minn. 393, 170 N. W. 343.

²⁸ *In re Canister Co.*, 248 Fed. 587, 589.

to issue a call on a subscriber for the balance of his subscription and to bring an action therefor cannot be collaterally attacked by the subscriber on the ground that it does not affirmatively appear that the money is necessary to pay creditors.²⁹ An order of a federal court in bankruptcy ordering an assessment against stock is not *res judicata*, in a suit to collect assessments by the trustee in bankruptcy, that stock was issued to a particular stockholder without consideration.³⁰ An order of a referee in bankruptcy requiring a subscriber to pay the balance due on his stock to the trustee in bankruptcy is not conclusive as to the rights of the subscriber when sued by the trustee.³¹

§ 4121. Remedies—General principles. The remedy for enforcing the statutory liability of stockholders to creditors, in Delaware, on unpaid stock, by a creditor's action at law or bill in chancery, is not exclusive, but the liability may be enforced by receivers in insolvency proceedings in which case a judgment and execution against the corporation is not a condition precedent.³² The burden of proof in an action by creditors against stockholders, for unpaid balances on their stock, is on plaintiff.³³

§ 4122. — Actions at law and suits in equity. A suit in equity does not lie in the federal courts to enforce liability on unpaid subscriptions in favor of creditors, since the remedy at law is adequate; and such a liability imposed by a state statute cannot be enforced in a federal court in an equity suit.³⁴ In South Carolina, an ancillary action by a receiver to collect unpaid stock subscriptions is a legal demand and need not be transferred to the equity calendar.³⁵

§ 4127. — Parties. Where a corporation is insolvent, one creditor cannot sue alone to collect unpaid subscriptions.³⁶ A bill by creditors to collect on unpaid subscriptions must join

²⁹ *Jeffery v. Selwyn*, 220 N. Y. 77, 115 N. E. 275, *aff'g* 173 N. Y. App. Div. 217, 159 N. Y. Supp. 430.

³⁰ *Sweet v. Barnard*, 66 Colo. 526, 182 Pac. 22.

³¹ *Martin v. Cushwa*, — W. Va. —, 104 S. E. 97.

³² *Du Pont v. Ball*, 11 Del. Ch. 430, 106 Atl. 39, modifying *John*

W. Cooney Co. v. Arlington Hotel Co., 11 Del. Ch. 286, 101 Atl. 879.

³³ *Donoho v. Carwile*, — Tex. Civ. App. —, 214 S. W. 553.

³⁴ *Clinton Mining & Mineral Co. v. Cochran*, 247 Fed. 449.

³⁵ *Buist v. William M. Bird & Co.*, — S. C. —, 99 S. E. 827.

³⁶ *John A. Roebling's Sons Co. v. Kinnicutt*, 248 Fed. 596.

the corporation as a party, although it has ceased to do business, where it has not been dissolved.³⁷ A bill by creditors in a federal court to enforce liability on unpaid stock subscriptions is not defective because of failure to join other stockholders acquiring stock at less than par, since they can be brought in by cross-bill, if within the jurisdiction.³⁸ In a suit under the New York statute by creditors to hold stockholders liable for the amount unpaid on their subscriptions, all the stockholders need not be sued, since the liability is several.³⁹ But where a receiver of an insolvent company is seeking to pay debts by collecting balances on unpaid stock, it is inequitable for him to collect the entire assessment from one resident stockholder but instead the receiver should collect every assessment found to be collectible.⁴⁰ Creditors of an insolvent corporation cannot sue a part of the stockholders without joining all unless those not joined are nonresidents or there is other good cause for their nonjoinder.⁴¹

§ 4129. — Exhausting legal remedies against corporation; judgment and execution. It is a good excuse for failure of a creditor to first recover judgment and have an execution returned unsatisfied against the corporation, before suing stockholders under the statute for the amount unpaid on their subscription, that the company had been dissolved or that the claims have been established against the corporation in a bankruptcy court; but it is no excuse that the corporation was declared a bankrupt and creditors enjoined from suing where it does not appear that the injunction was in force at the time the action against the stockholders was brought.⁴² A receiver need not exhaust the remedies of the corporation against corporate officers for wrongdoing before suing stockholders to collect their subscriptions.⁴³

³⁷ Clinton Mining & Mineral Co. v. Cochran, 247 Fed. 449.

³⁸ Second Nat. Bank v. Georger, 246 Fed. 517.

³⁹ John A. Roebling's Sons Co. of New York v. Federal Storage Battery Car Co., 185 N. Y. App. Div. 430, 173 N. Y. Supp. 297.

⁴⁰ Du Pont v. Ball, 11 Del. Ch. 430, 106 Atl. 39, modifying John

W. Cooney Co. v. Arlington Hotel Co., 11 Del. Ch. 286, 101 Atl. 879.

⁴¹ M. A. Gedney Co. v. Sanford, — Neb. —, 179 N. W. 385.

⁴² John A. Roebling's Sons Co. of New York v. Federal Storage Battery Car Co., 185 N. Y. App. Div. 430, 173 N. Y. Supp. 297.

⁴³ Preston v. Jeffers, 179 Ky. 384, 200 S. W. 654.

§ 4130. — Conclusiveness of judgment against corporation as against stockholders. A judgment in an action against a corporation on a guaranty, deciding that it was not *ultra vires*, is binding on a stockholder in an action by the creditor against a stockholder to recover to the extent of unpaid subscriptions.⁴⁴ A judgment against a corporation on notes secured by chattel mortgage is conclusive as to the validity of the notes, in an action to enforce stockholders' liability for unpaid subscriptions.⁴⁵

§ 4131. — Enforcing liability in other states. After an assessment of stockholders is made by a court in the state where the corporation was created, the assessment may be enforced against nonresident stockholders by actions in sister states.⁴⁶

§ 4132. Set-off of debts due to stockholders.⁴⁷ A creditor of a bankrupt company who is liable as a stockholder for calls or assessments cannot participate in the assets until he has paid or satisfied such calls or assessments.⁴⁸ Deposits cannot be set off in an action by a receiver against a stockholder.⁴⁹ The doctrine of marshalling assets is properly applied in favor of a creditor seeking to hold a stockholder liable for unpaid balances, where the latter pleads a set-off on his first block of stock and the two blocks constitute separate funds.⁵⁰

§ 4133. Application of the statute of limitations—General principles. Within statutes of limitation, the liability of a stockholder for corporate debts, to the amount unpaid on the par value of his stock, is not "created by statute" nor "created by law" within the three-year limitation, but is a debtor's obligation created by the contract of subscription.⁵¹ Actions in

⁴⁴ *Keyes v. Baskerville*, 41 S. D. 214, 175 N. W. 874.

⁴⁵ *Barnard v. McIntire*, — Cal. App. —, 187 Pac. 440.

⁴⁶ *Chicago Title & Trust Co. v. Young's Ex'rs*, 90 N. J. Eq. 27, 105 Atl. 601.

⁴⁷ Note on "right of stockholder after insolvency to set off debt due him from corporation against his liability on unpaid

stock subscription," see *L. R. A.* 1918 E 243.

⁴⁸ *In re Manufacturers' Box & Lumber Co.*, 251 Fed. 957.

⁴⁹ *Swicord v. Crawford*, 23 Ga. App. 522, 98 S. E. 817.

⁵⁰ *Keyes v. Baskerville*, 41 S. D. 214, 175 N. W. 874.

⁵¹ *Jensen v. Aikman*, 32 Idaho 261, 181 Pac. 525.

An action by a creditor of a

favor of creditors against stockholders for unpaid balance on stock are barred in Colorado in six years.⁵²

§ 4134. — Accrual of right of action. A call is necessary to start limitations running.⁵³ Limitations begin to run not when the call is made but when the assessment is made.⁵⁴ A cause of action on unpaid subscriptions does not accrue in favor of a receiver until the order of court fixing the amount of the assessment and directing the receiver to sue.⁵⁵ Under a statute making the balance over ten per cent of stock subscriptions due at such time as the directors require its payment, the cause of action to recover unpaid instalments over and above the ten per cent, where a receiver has been appointed, accrues at the time of the order of court requiring payment, where the directors have never demanded payment.⁵⁶

So far as the liability of stockholders to creditors for the amount unpaid on their stock is concerned, limitations ordinarily begin to run from the time the claims of the creditors against the corporation mature and not from the time of the purchase of the stock.⁵⁷

XXXIV. PERSONAL LIABILITY OF STOCKHOLDERS FOR DEBTS OF THE CORPORATION

§ 4137. Liability in the absence of charter, statutory or constitutional provisions—General principles. This general rule as to nonliability of stockholders for corporate debts applies equally well to stockholders in de facto corporations.⁵⁸

corporation to recover from a shareholder because of a balance due upon his stock, whether based on the common law or a statute merely recognizing such common-law liability, is not an action "to enforce a liability created by law" so as to be barred in three years. *Feehan v. Kendrick*, 32 Idaho 220, 179 Pac. 507.

⁵² *Sweet v. Barnard*, 66 Colo. 526, 182 Pac. 22.

⁵³ *In re Phoenix Hardware Co.*, 249 Fed. 410; *Grice v. Anderson*, 109 S. C. 388, 96 S. E. 222.

⁵⁴ *Sweet v. Barnard*, 66 Colo. 526, 182 Pac. 22.

⁵⁵ *Thomas v. Kalbfus*, 97 Ohio St. 232, 119 N. E. 412.

⁵⁶ *Thomas v. Kalbfus*, 97 Ohio St. 232, 119 N. E. 412.

⁵⁷ *Shugart v. Maytag*, — Iowa —, 176 N. W. 886, holding this to be the rule under the South Dakota statutes.

⁵⁸ *Pocahontas Fuel Co. v. Tarboro Cotton Factory*, — N. C. —, 93 S. E. 790.

Sometimes, however, a stockholder is liable where he is in effect the corporation,⁵⁹ or where he appropriates all the corporate assets to his individual use, in which case he is personally liable for corporate debts to the extent of such assets.⁶⁰ Thus one who purchased and became the owner of all the capital stock of a corporation and thereafter commingled its assets with other like property of his own and converted it to his own use, leaving nothing to the corporation with which to pay its debts, is personally liable for corporate indebtedness, including corporate taxes.⁶¹

Where a corporation sold all its property and distributed the proceeds among its stockholders, pending criminal proceedings against it resulting in a fine, the fine may be collected by a creditor's suit against the stockholders to the extent of the proceeds received by them, regardless of the fact that the purchaser assumed all debts and liabilities.⁶² Creditors of a corporation may sue stockholders to compel them to account for corporate assets divided among themselves when the corporation ceased to do business; and the liability of the stockholders is limited to the value of the proceeds each one received and, as between the several stockholders, contribution should be made pro rata for the satisfaction of the corporate debt.⁶³

⁵⁹ An action against the individual owner of practically all the stock of a corporation, to compel the payment of an unsatisfied judgment against the corporation, while unusual, lies where he is estopped to deny the debt is his because of his holding himself out as the corporation, on the theory of the right of a court of equity to refuse to permit a mere corporate entity, found to be a sham, to be used as an instrument for fraud. *Quaid v. Ratkowsky*, 183 N. Y. App. Div. 428, 170 N. Y. Supp. 812, and see § 42 et seq., supra.

⁶⁰ *Fulton Auto Supply Co. v. Sullivan*, 148 Ga. 347, 96 S. E. 875.

It is proper to award a personal judgment for corporate taxes against a stockholder, where he has appropriated all the corporate assets to his own use, to evade payment of corporate debts. *Martin v. Com.*, 181 Ky. 212, 204 S. W. 84.

⁶¹ *Martin v. City of Lexington*, 183 Ky. 714, 210 S. W. 483.

⁶² *Pierce v. United States*, 257 Fed. 514, citing *Swan Land & Cattle Co. v. Frank*, 148 U. S. 603, 37 L. Ed. 577.

⁶³ *Adams v. Perryman & Co.*, 202 Ala. 469, 80 So. 853. To same effect, *Martin v. City of Lexington*, 183 Ky. 714, 210 S. W. 483.

§ 4138. — **Liability for torts.** A stockholder is not individually liable for profits arising from corporate infringement of a trade-mark, in excess of the share of such profits he receives.⁶⁴

§ 4140. — **Agreement or consent of stockholders.**⁶⁵ Future advances to be made to the corporation is a sufficient consideration for a guaranty by stockholders of corporate debts.⁶⁶ A guaranty of a corporate debt by a stockholder who is also a large creditor is based on a consideration even though it be conceded the entire benefit accrued to the corporation.⁶⁷ A stockholder who pays a corporate debt at its request is subrogated to a lien securing the debt.⁶⁸

In California, under its statutes, an agreement by a director to be primarily liable for the payment of a certain sum to settle a claim against the corporation for a larger sum, is an original promise and need not be in writing.⁶⁹

§ 4141. **Statutory liability in general.** "Statutory liability" of stockholders generally refers to double or additional liability laws as distinguished from liability imposed by statute in favor of creditors for the balance of unpaid subscriptions.⁷⁰ The statutory liability of stockholders depends primarily on the existence of corporate liability.⁷¹ Under the Kentucky statutes governing insurance companies, the liability of subscribers to stock therein, so far as creditors are concerned, is not affected by the failure of the company to secure from the insurance commissioner permission to do business.⁷²

⁶⁴ *Prest-O-Lite Co. v. Bournonville*, 260 Fed. 446.

⁶⁵ See also § 40, *supra*.

Construction of guaranty of payment of principal and dividends on stock, by other stockholders, see *Weiss v. Sullivan*, — N. J. L. —, 109 Atl. 344.

⁶⁶ *McGowan v. Wells' Trustee*, 184 Ky. 772, 213 S. W. 573.

⁶⁷ *International Harvester Co. v. Patterson*, 257 Fed. 411.

⁶⁸ *United States Cast Iron Pipe & Foundry Co. v. Henry Vogt*

Mach. Co., 182 Ky. 473, 206 S. W. 806.

⁶⁹ *Fairchild v. Cartwright*, 39 Cal. App. 118, 178 Pac. 333.

⁷⁰ *Du Pont v. Ball*, 11 Del. Ch. 430, 106 Atl. 39, modifying *John W. Cooney Co. v. Arlington Hotel Co.*, 11 Del. Ch. 286, 101 Atl. 879.

⁷¹ *Huey v. Patterson*, 37 Cal. App. 335, 174 Pac. 939.

⁷² *Levassor v. Metropolitan Fire Ins. Co.'s Receiver*, 188 Ky. 23, 220 S. W. 752.

§ 4142. Effect of constitutional provisions. A statute making stockholders liable for corporate debts to the extent of the amount unpaid on their stock does not violate constitutional provisions forbidding issuance of stock except for money, labor done or property actually received.⁷³

§ 4143. Whether constitutional provisions are self-executing. Constitutional provisions imposing double liability on stockholders are often self-executing.⁷⁴ A constitutional provision excepting from limited liability, and making them liable to the amount of their stock, stockholders of corporations "authorized to receive money on deposit" is self-executing.⁷⁵

§ 4146. Alteration or repeal of constitutional or statutory provisions—Effect as against stockholders. Where there is no reserved power to alter the charter, a statute passed subsequently to the creation of a corporation, and increasing the liability of stockholders on their stock for debts of the corporation, is invalid as violating the obligation of a contract; and this is so although the new statute was passed before the subscription to stock.⁷⁶

§ 4148. Effect of reorganization of corporation. Statutory exemption of stockholders from liability in excess of unpaid subscriptions is lost, it seems, by reincorporating under a statute allowing no such exemption.⁷⁷

§ 4149. Effect of consolidation of corporations. Statutory exemption of liability of stockholders of one constituent company does not, it seems, pass to a stockholder of the other constituent company as a stockholder of the new consolidated company.⁷⁸

§ 4151. Conflict of laws. The liability of a stockholder is governed by the laws of the state where the company was

⁷³ Shugart v. Maytag, — Iowa —, 176 N. W. 886.

⁷⁴ Austin v. Campbell, — Tex. Civ. App. —, 210 S. W. 277; Lynch v. Jacobsen, — Utah —, 184 Pac. 929, citing Fletcher Cyc. Corp. § 4143.

⁷⁵ Lang v. Osborn Bank, 100 Ohio St. 51, 125 N. E. 105.

⁷⁶ First Nat. Bank v. Multnomah State Bank, 87 Ore. 423, 170 Pac. 534.

⁷⁷ Johnson v. Barton, — Fla. —, 83 So. 722.

⁷⁸ Johnson v. Barton, — Fla. —, 83 So. 722.

created.⁷⁹ The liability of a Canadian stockholder in a corporation created in the United States, as imposed by a state constitution or statutes, is governed by the law of such state.⁸⁰

§ 4155. Extent of liability—Liability in proportion to amount or value of stock. Payment to the corporation of more than the par value of the stock cannot be credited on the statutory double liability.⁸¹

§ 4156. — Liability until payment or subscription of capital stock. A claim for damages for breach of a lease is a "debt" within a statute providing that persons who organize a company and transact business in its name before the minimum capital stock has been subscribed for are liable to creditors to make good the minimum capital stock with interest.⁸² This statute applies to banks as well as other corporations.⁸³ The statutory liability to creditors of organizers of a corporation for transacting business in its name before the minimum capital stock has been subscribed for, does not exist where the creditor has knowledge of the facts at the time he extends the credit.⁸⁴

§ 4157. — Liability on failure to file report or statement. Sometimes the statute makes stockholders individually liable for failure to file an annual report. The statute in Nebraska making stockholders individually liable for debts where the corporation fails to file its annual notice of indebtedness, is constitutional.⁸⁵

§ 4158. — Liability because of defective organization. Omitting to definitely state in the articles of incorporation the highest amount of debts the corporation may incur is, in Iowa, within

⁷⁹ Zehr v. Zehr, 203 Ill. App. 584, 595.

⁸⁰ Allen v. Standard Trust Co., 49 Dom. L. Rep. (Can.) 399.

⁸¹ Skinner v. Schwab, 188 N. Y. App. Div. 457, 177 N. Y. Supp. 143.

⁸² American Ice Cream Mfg. Co. v. Economy Laundry Co., 148 Ga. 624, 97 S. E. 678.

⁸³ Smith v. Citizens' & Southern Bank, 148 Ga. 764, 98 S. E. 466.

⁸⁴ Farmers' Warehouse & Fertilizer Co. v. Macon Fertilizer Works, — Ga. —, 104 S. E. 207.

⁸⁵ Spear v. Olson, — Neb. —, 175 N. W. 1012.

the statute providing that "a failure to substantially comply with the foregoing requirements in relation to organization and publicity shall render the individual property of the stockholders liable for the corporate debts."⁸⁶

§ 4161. What corporations are within statutory or constitutional provisions—In general. Statutes in some states apply to banks as well as other corporations.⁸⁷ The constitutional provision in New York imposing double liability on stockholders of every banking corporation applies to a corporation having the powers of a trust company.⁸⁸

§ 4162. — Provisions excepting certain classes of corporations. The exemption of stockholders from statutory liability in case of manufacturing or mechanical corporations applies only to companies exclusively engaged in manufacturing or mechanical business, to be determined by the articles of incorporation.⁸⁹

§ 4163. Liabilities to which the statutory or constitutional provisions apply—In general. Advances by certain stockholders are debts which may be enforced against the stockholders at large, in enforcing their statutory liability; and this is so although it was stipulated that the note given therefor should be paid "from sales of merchandise or from sales of the treasury stock of the corporation."⁹⁰

§ 4164. — Liabilities based upon tort. Statutory liability of stockholders "for debts of the corporation" does not include liability for torts.⁹¹ Reducing a claim for a tort to judgment

⁸⁶ *Parsons v. Rinard Grain Co.*, — Iowa —, 173 N. W. 276.

⁸⁷ The Georgia statute making organizers of corporations liable to creditors where they transact business in the corporate name before the minimum capital stock has been subscribed applies to banks as well as other private corporations. *Smith v. Citizens' & Southern Bank*, 148 Ga. 764, 98 S. E. 466.

⁸⁸ *Skinner v. Schwab*, 188 N. Y.

App. Div. 457, 177 N. Y. Supp. 143.

⁸⁹ *Graff v. Minnesota Flint Rock Co.*, — Minn. —, 179 N. W. 562.

Minnesota exemption of manufacturing corporations, see also *Marin v. Augedahl*, 247 U. S. 142, 62 L. Ed. 1038, rev'g 32 N. D. 536, 156 N. W. 101.

⁹⁰ *Huey v. Patterson*, 37 Cal. App. 335, 174 Pac. 939.

⁹¹ *Clinton Mining & Mineral*

does not affect liability of stockholders where limited to liability for debts and not including torts.⁹² Statutory liability of stockholders extends, in California, to liability arising out of a tort.⁹³

§ 4165. — Liabilities arising out of contract. Under the rule that stockholders are not liable under the statute, for failure to file the annual notice of indebtedness, for debts incurred before the corporation was in default in publishing the notice, they are not liable where the original indebtedness was incurred before the default, though the debt was renewed and new notes given after the default.⁹⁴

§ 4172. — Liability dependent upon maturity of debt or time of bringing suit against corporation. The statutory double liability covers only liabilities incurred during the period of ownership of the stock by the person sought to be held liable.⁹⁵

In New York, the statutory liability of stockholders to creditors for unpaid subscriptions attaches only to debts contracted while a stockholder holds stock and which are payable in two years; and a creditor cannot rely on a judgment, since it is not conclusive on such points.⁹⁶

§ 4177. Whether the liability is that of sureties or guarantors.⁹⁷

§ 4180. Whether the liability is primary or secondary. In California, the liability of stockholders to creditors is primary, and not affected by the creditor holding a guaranty of the corporate debt.⁹⁸ In West Virginia, the double liability is not a primary but a secondary liability and limitations do not begin to run until the necessity for payment is ascertained.⁹⁹ The statu-

Co. v. Beacom, 266 Fed. 621, 264 Fed. 228, construing South Dakota statute.

⁹² Clinton Mining & Mineral Co. v. Beacom, 266 Fed. 621, 264 Fed. 228.

⁹³ Damiano v. Bunting, — Cal. App. —, 181 Pac. 232.

⁹⁴ Spear v. Olson, — Neb. —, 175 N. W. 1012.

⁹⁵ Heater v. Lloyd, — W. Va. —, 102 S. E. 228.

⁹⁶ Graeber v. Ehr Gott, 182 N. Y. App. Div. 377, 169 N. Y. Supp. 32.

⁹⁷ See § 4231, *infra*.

⁹⁸ Seaboard Nat. Bank of San Francisco v. Belden, — Cal. App. —, 190 Pac. 1045.

⁹⁹ Pyles v. Carney, — W. Va. —, 101 S. E. 174.

tory liability of bank stockholders in Washington is not an original but a secondary liability.¹

§ 4182. Persons liable—In general. It is no defense to enforcing double liability that a stockholder purchased his stock while insane, where no disaffirmance of the purchase is shown.² In an action by a receiver against a stockholder for double liability, fraud inducing the purchase of his stock is no defense.³

§ 4184. — Registered owners. One whose name appears on the books as a stockholder is liable although he in fact is not a stockholder.⁴

§ 4191. — Real and apparent owner; trustees, agents, executors, etc.—General rules. Where a wife refused to accept stock transferred to her by her husband without her consent, she is not liable as a stockholder to creditors, under the statute, although the stock is in her name on the books of the corporation. It is immaterial that she indorsed the certificate to have it transferred on the books back to her husband.⁵ There is an extended note on the "Liability of one whose name appears upon corporate books as a stockholder without his consent" in a recent volume of annotated cases.⁶

§ 4193. — Pledgees. Persons holding stock as collateral security for a debt not liable, under the bank statute, as a stockholder, for corporate debts.⁷ Persons holding voting trust certificates as collateral are not stockholders subject to statutory liability for corporate debts.⁸

¹ *Fremont State Bank v. Vincent*, — Wash. —, 192 Pac. 975.

² *Skinner v. Schwab*, 188 N. Y. App. Div. 457, 177 N. Y. Supp. 143.

³ *Bundy v. Wilson*, — Colo. —, 180 Pac. 740.

⁴ *Harris v. Taylor*, 148 Ga. 663, 98 S. E. 86.

⁵ *Shean v. Cook*, — Cal. —, 3 A. L. R. 1042 with note, 179 Pac. 185.

⁶ 3 A. L. R. 1049, annotating *Shean v. Cook*, — Cal. —, 3 A. L. R. 1042, 179 Pac. 185.

⁷ *Skinner v. Sullivan*, 190 N. Y. App. Div. 187, 179 N. Y. Supp. 567.

⁸ *Skinner v. Sullivan*, 190 N. Y. App. Div. 187, 179 N. Y. Supp. 567.

§ 4195. — Estates of deceased stockholders; distributees. The statutory liability of stockholders survives their death.⁹

§ 4196. — Effect of transfers of stock—In general.¹⁰ In Georgia, either the stockholder of record or the real owner of the stock may be sued to recover double liability.¹¹ A sale of stock by a stockholder by fraudulent representations does not prejudice the rights of the corporation or its creditors against the buyer as a stockholder.¹²

§ 4197. — Time when debt was contracted; renewal or change in character of debt. Generally the statutory liability of stockholders is not limited to debts contracted while they were stockholders.¹³ In Florida, where partnership liability is imposed by statute on stockholders, the liability for a debt is limited to those who were stockholders at the time the debt was incurred.¹⁴

§ 4199. — Statutory regulations. Under some statutes, stockholders who transferred their stock within less than one year prior to the default of the corporation, are liable.¹⁵ There is no "debt contracted" so as to make stockholders liable to creditors on unpaid subscriptions, under section 56 of the New York Stock Corporation Law, where the corporation obtains the right to make and sell a patented article in consideration of an agreement to pay royalties, until royalties become due.¹⁶ It is generally held that a sum payable upon a contingency is not presently a debt and does not become a debt until the contingency has happened, so that stockholders are not liable for such sums under statutes making them liable for "debts contracted" while they owned the stock.¹⁷

⁹ *Damiano v. Bunting*, — Cal. App. —, 181 Pac. 232; *Skinner v. Sullivan*, 112 N. Y. Misc. 365, 184 N. Y. Supp. 159.

¹⁰ See *Conley v. Hunt*, — Conn. —, 109 Atl. 887, stating California law.

¹¹ *Harris v. Taylor*, 148 Ga. 663, 98 S. E. 86.

¹² *Romunder v. Caskey*, 137 Ark. 574, 209 S. W. 735.

¹³ *Bundy v. Wilson*, — Colo. —, 180 Pac. 740.

¹⁴ *Mechanics & Metals Nat. Bank v. Angel*, — Fla. —, 85 So. 675.

¹⁵ *Austin v. Campbell*, — Tex. Civ. App. —, 210 S. W. 277.

¹⁶ *Bottlers' Seal Co. v. Rainey*, 225 N. Y. 369, 122 N. E. 200.

¹⁷ *Bottlers' Seal Co. v. Rainey*, 225 N. Y. 369, 122 N. E. 200, rev'g

§ 4200. — — **Transfer by stockholder who has satisfied liability.** If a holder of shares of stock has paid the full statutory liability, then of course no other holder of the same stock can be held liable.¹⁸

§ 4201. — — **Transfers to escape liability or which are merely colorable.** A stockholder cannot evade his statutory liability by transferring his stock.¹⁹

§ 4205. — — **Registration of transfers.** A registered stockholder is not liable for the statutory liability where he had sold the stock long before in good faith and there was no neglect on his part in having the transfer registered.²⁰

§ 4208. — **Evidence and burden of proof.** Although a statute puts the burden of proof on creditors, in actions to hold stockholders liable for corporate debts, to show that defendants were stockholders at the time the debt was incurred, proof that they were stockholders in 1912, although the debts were incurred in 1913 and 1915, has been held sufficient, on the theory of a presumption of continuance of conditions.²¹

§ 4209. — **Estoppel.** There is no estoppel to deny ownership of stock appearing on the corporate books in the name of a person, as against creditors seeking to enforce statutory liability, where they did not know at the time credit was extended that he was a stockholder on the books.²²

§ 4211. **Who may enforce liability—Creditors who are also stockholders in the corporation.** A creditor stockholder is not entitled to recover against other stockholders for failure of the corporation to publish the annual notice of indebtedness as required by statute, since he is equally guilty with the other stockholders.²³

180 N. Y. App. Div. 935, 167 N. Y. Supp. 1091.

¹⁸ Pyles v. Carney, — W. Va. —, 101 S. E. 174.

¹⁹ Fremont State Bank v. Vincent, — Wash. —, 192 Pac. 975.

²⁰ Keyes v. Myhre, 143 Minn. 193, 173 N. W. 422.

²¹ Huey v. Patterson, 37 Cal. App. 335, 174 Pac. 939.

²² Shean v. Cook, — Cal. —, 3 A. L. R. 1042, 179 Pac. 185.

²³ Singhaus v. Piper, 103 Neb. 493, 172 N. W. 523, followed in Spear v. Olson, — Neb. —, 175 N. W. 1012.

§ 4214. — Receivers, trustees in bankruptcy, assignees for creditors, etc. In most jurisdictions, a receiver for the corporation may sue to enforce the liability of stockholders for corporate debts.²⁴ Stockholders sued by a receiver for corporate debts cannot for the first time attack the jurisdiction of the court to appoint the receiver.²⁵

§ 4216. Mode of enforcing liability—General principles. Admiralty has jurisdiction of a cause of action to recover damages for personal injuries resulting from a marine tort, against stockholders made, by state statute, directly answerable for corporate debts.²⁶

§ 4217. — Remedy prescribed by statute. The legislature may fix the remedy where a self-executing constitutional provision imposing double liability on stockholders makes no provision as to the remedy.²⁷ But state statutes providing a remedy for collecting unpaid stock subscriptions in favor of creditors of an insolvent corporation do not furnish an exclusive remedy nor supersede the equitable remedy independent of statute.²⁸

§ 4218. — Actions at law and suits in equity. The equity jurisdiction of federal courts is not enlarged by state statutes providing an equitable remedy for the enforcement in favor of creditors of stockholder's liability for unpaid subscriptions.²⁹ In Georgia, a suit by a receiver against stockholders on their statutory liability is one in equity.³⁰ An action by a creditor against a stockholder to recover the amount of his debt, under the Wisconsin statute, because business was transacted before half of the stock had been subscribed, is properly treated as

²⁴ Harris v. Taylor, 148 Ga. 663, 98 S. E. 86; Davis v. Johnson, — N. D. —, 170 N. W. 520, bank; Lynch v. Jacobsen, — Utah —, 184 Pac. 929.

Sufficiency of complaint in action by receiver to enforce double liability of stockholders, see Lynch v. Jacobsen, — Utah —, 184 Pac. 929.

²⁵ Bartlett v. Taylor, 148 Ga. 854, 98 S. E. 491.

²⁶ Buttner v. Adams, 236 Fed. 105.

²⁷ Lynch v. Jacobsen, — Utah —, 184 Pac. 929.

²⁸ Second Nat. Bank v. Georger, 246 Fed. 517.

²⁹ Second Nat. Bank v. Georger, 246 Fed. 517.

³⁰ Taylor v. Lamar, 148 Ga. 660, 97 S. E. 858; Buttrill v. Taylor, 148 Ga. 671, 97 S. E. 860.

one at law rather than in equity, the liability being primary and not secondary.³¹

§ 4223. — Assessment by court. A referee in bankruptcy cannot assess stock a hundred per cent, where the corporation owns much valuable property, merely because he cannot reach a satisfactory conclusion as to what proportion of each share was liable to assessment.³²

§ 4227. — Parties—In actions at law. In an action to enforce the statutory liability of stockholders, all of the stockholders may be joined as defendants.³³ A stockholder against whom statutory liability is enforced for his share of a corporate debt cannot complain of such a judgment instead of a judgment for the entire debt against all the stockholders.³⁴ Executors or administrators of deceased stockholders should be made defendants in actions to enforce statutory liability of stockholders.³⁵ The corporation is not a necessary defendant in a suit by its only creditor against its only stockholder to hold the latter liable individually for a corporate debt, where the corporation has no business, assets, officers or agent.³⁶

§ 4231. Necessity for exhausting assets of the corporation and remedies against it—General principles. In Idaho, exhausting the remedy against the corporation is necessary before suing a stockholder on his statutory liability.³⁷ In Kansas, a stockholder is not liable for corporate debts in an action on a claim not reduced to judgment.³⁸

§ 4232.—Excuses for failure to exhaust remedies against corporation. If the corporation is insolvent, all the corporate

³¹ Shadbolt & Boyd Iron Co. v. Long, — Wis. —, 179 N. W. 785.

³² In re Canister Co., 252 Fed. 70.

³³ Harris v. Taylor, 148 Ga. 663, 98 S. E. 86.

A receiver may sue as many of the stockholders in one action as he sees fit, to recover double liability. Lynch v. Jacobsen, — Utah —, 184 Pac. 929.

³⁴ Parsons v. Rinard Grain Co., — Iowa —, 173 N. W. 276.

³⁵ Pyles v. Carney, — W. Va. —, 101 S. E. 174.

³⁶ Louisville & N. R. Co. v. Nield, 186 Ky. 17, 216 S. W. 62.

³⁷ Weil v. Defenbach, 31 Idaho 258, 170 Pac. 103.

³⁸ Jones v. Citizens' State Bank, 103 Kan. 297, 173 Pac. 977.

assets need not be first exhausted before suing stockholders.³⁹ Judgment against the corporation and an execution returned *nulla bona* is not a condition to an action by a creditor against a stockholder to recover a corporate debt, where the stockholder, owning all the stock, has appropriated all the corporate assets to his own use.⁴⁰ Where there is only one creditor and only one stockholder, and the latter has by his fraudulent act made an independent action against the corporation an impractical and vain undertaking involving circuitry of action and unnecessary delay and expense, a judgment against the corporation is not a condition precedent to a creditor's suit against the stockholder.⁴¹

The Kentucky Court of Appeals joins with the courts of New York and Ohio, as against the federal courts and the courts of Massachusetts and Tennessee, in holding that a *de jure*, as distinguished from a *de facto*, dissolution of a corporation is necessary to excuse a creditor in failing to prosecute his demand to judgment against the corporation before proceeding to charge the stockholders.⁴² The New York statute requires creditors to obtain a judgment and a return of execution unsatisfied before suing stockholders for the amount unpaid on their stock; and it is no excuse that the corporation has been adjudicated a bankrupt and the creditors enjoined from suing where it does not appear that the injunction was still in force when the action against the stockholders was commenced. On the other hand, it is an excuse for not suing that the corporation was dissolved by the bankruptcy court or that the claims have been allowed against the corporation in the bankruptcy court.⁴³

§ 4236. Conclusiveness of judgment against corporation as against stockholders. In Texas, in a suit by a judgment creditor of a corporation against a stockholder therein to establish liability for the debt, the judgment against the corporation is con-

³⁹ *Lynch v. Jacobsen*, — Utah —, 184 Pac. 929.

⁴⁰ *Fulton Auto Supply Co. v. Sullivan*, 148 Ga. 347, 96 S. E. 785.

⁴¹ *Louisville & N. R. Co. v. Nield*, 186 Ky. 17, 216 S. W. 62.

⁴² *Louisville & N. R. Co. v. Nield*, 186 Ky. 17, 216 S. W. 62.

⁴³ *John A. Roebling's Sons Co. of New York v. Federal Storage Battery Car Co.*, 185 N. Y. App. Div. 430, 173 N. Y. Supp. 297.

clusive evidence of the debt.⁴⁴ An adjudication that a contract was not *ultra vires*, in an action against a corporation, is binding on a stockholder sued on his statutory liability for the amount unpaid on his stock.⁴⁵

§ 4237. Conclusiveness of order or decree assessing stockholders.⁴⁶ An order declaring it necessary to enforce stockholders' liability on account of the insolvency of the corporation is conclusive on the stockholders.⁴⁷ But an order of a bankruptcy court assessing stockholders on unpaid stock is not conclusive as to whether the stock is full paid.⁴⁸

An assessment order made by a Minnesota Court in a sequestration suit against a Minnesota corporation, made conclusive by statute "as to all matters relating to the amount, propriety and necessity of the assessment," cannot be collaterally attacked on the ground that the corporation is not such a one as is within the statute imposing double liability on stockholders; and this applies also to a collateral attack in another state.⁴⁹

§ 4238. Application of the statute of limitations—General principles. In South Carolina, by statute, actions by or in behalf of creditors to enforce the statutory liability of stockholders for unpaid subscriptions, in case of a "moneyed" corporation, must be brought within six years.⁵⁰ The statutory liability of stockholders must be enforced, under the California statute, within three years.⁵¹

⁴⁴ *Butcher v. J. I. Case Threshing Mach. Co.*, — Tex. Civ. App. —, 207 S. W. 980.

⁴⁵ *Keyes v. Baskerville*, 41 S. D. 214, 175 N. W. 874.

⁴⁶ See also § 4120, *supra*.

Action of bank commissioner in levying assessments on stockholders as conclusive as to necessity for call and amount thereof, see *Aber v. Maxwell*, 140 Ark. 203, 215 S. W. 389.

⁴⁷ *Lynch v. Jacobsen*, — Utah —, 184 Pac. 929.

⁴⁸ *Sweet v. Barnard*, 66 Colo. 526, 182 Pac. 22.

⁴⁹ *Marin v. Augedahl*, 247 U. S. 142, 62 L. Ed. 1038, rev'g 32 N. D. 536, 156 N. W. 101, the gist of the lower court's holding being stated *contra* on pp. 7428 and 7429.

⁵⁰ *Grice v. Anderson*, 109 S. C. 388, 96 S. E. 222, holding an investment company a "moneyed" corporation.

⁵¹ *Damiano v. Bunting*, — Cal. App. —, 181 Pac. 232.

It is a "liability created by law." *Chambers v. Farnham*, — Cal. —, 187 Pac. 732.

§ 4239. — Accrual of right of action and running of the statute. In some jurisdictions, stockholders' statutory liability accrues at the inception of corporate liability and not at the time such liability is sought to be enforced against the corporation.⁵² In Kansas, the cause of action on a double liability, in case of corporate insolvency, accrues when the fact of insolvency and the extent of the liability are determined.⁵³ In New York, by statute, the double liability of stockholders in banks and trust companies (the latter being included within the term "bank") is barred in three years, and the cause of action accrues, at least in equity, as soon as the necessity to resort to stockholders exists.⁵⁴

Limitations do not run in favor of stockholders sued by creditors, where the creditor's claim is based on an implied contract to repay money because of its rescission of the contract because of acts of the corporation, until election by the creditor to treat the act of the corporation as a rescission.⁵⁵

§ 4240. — Interruption or tolling of statute. A judgment against the corporation or the time consumed in taking an appeal

⁵² *Smith v. Pillsbury*, 39 Cal. App. 240, 178 Pac. 719.

An action against stockholders for corporate debts is one on a "liability created by law" so as to be barred in three years from the incurring of the debt rather than three years from the rendition of judgment against the corporation. *Chambers v. Farnham*, — Cal. —, 187 Pac. 732.

A cause of action against stockholders for a corporate tort arises at the same time the cause of action arises against the corporation, and not when a judgment is recovered against the corporation. *Douglas v. Orth*, — Cal. App. —, 185 Pac. 1005.

A claim against stockholders, based on payment by an indorser of a corporate note and an assign-

ment of the note, arises at the time of such payment, within the statute of limitations. *Huey v. Patterson*, 37 Cal. App. 335, 174 Pac. 939.

In one case it is held that the statutory liability of stockholders to corporate creditors accrues when the corporation made the contract out of which the liability arises and not at the time of breach by the corporation. *Pidgeon v. San Diego Consol. Brewing Co.*, — Cal. App. —, 190 Pac. 1048.

⁵³ *Davis v. Drury*, 105 Kan. 69, 181 Pac. 559.

⁵⁴ *Richards v. Carpenter*, 261 Fed. 724.

⁵⁵ *Kempton v. Floribel Land & Improvement Co.*, — Cal. App. —, 189 Pac. 478.

does not extend the time for suing stockholders for corporate debts or liabilities.⁵⁶

§ 4246. Set-off of debts due to stockholders. In enforcing statutory liability of a stockholder on unpaid stock, where he had bought stock at different times and had a set-off as to some of the stock, the doctrine of marshalling assets may be applied.⁵⁷

§ 4253. Enforcing liability in other states—Right of receivers, etc., to sue in foreign state. A receiver, where he has no greater rights than a chancery receiver, cannot sue in a sister state to enforce the double statutory liability of stockholders.⁵⁸

§ 4265. Discharge of stockholders; waiver, release and payment—Insolvency or bankruptcy proceedings with respect to stockholder. A stockholder's discharge in bankruptcy relieves him of his liability for debts of the company although he filed his petition in bankruptcy after the company had become insolvent.⁵⁹

§ 4266. Contribution among stockholders. A stockholder who pays a corporate debt is entitled to contribution from the other stockholders.⁶⁰

XXXV. ASSESSMENT ON FULL PAID STOCK

§ 4270. Right to levy assessments generally.⁶¹ A by-law providing that no assessment shall be levied while any portion of the previous one remains unpaid unless the power of the corporation shall have been exercised to collect it does not exempt a stockholder who fails to pay an assessment from any further assessment.⁶²

⁵⁶ Douglas v. Orth, — Cal. App. —, 185 Pac. 1005.

⁵⁷ Keyes v. Baskerville, 41 S. D. 214, 175 N. W. 874.

⁵⁸ Miller v. Amoretti, — Wyo. —, 181 Pac. 420.

⁵⁹ Richards v. Schwab, 101 N. Y. Misc. 128, 167 N. Y. Supp. 535, following Van Tuyl v. Schwab, 174 N. Y. App. Div. 665, 161 N.

Y. Supp. 323, aff'd without opinion in 220 N. Y. 661, 116 N. E. 1081.

⁶⁰ Holyfield v. Davis, 139 Ark. 479, 214 S. W. 53.

⁶¹ See also § 4279, infra.

⁶² Pennecard v. Giant Ledge Min. Co., 97 Wash. 384, 166 Pac. 629.

§ 4272. Power conferred by charter or statute. Where the articles of incorporation authorize an assessment on stock, it may be levied, notwithstanding the stock is full paid.⁶³ In case of state banks, under the Minnesota statutes, the stockholders, and not the board of directors, are to elect whether, in case the capital becomes impaired, to go into liquidation or assess the stock; and the directors have no power to assess the stock.⁶⁴

§ 4273. Purpose and amount of assessment; conditions precedent. An assessment is not invalid because made to freeze out a certain stockholder or stockholders, since the motive of an assessment is immaterial.⁶⁵

§ 4274. Persons liable; rights and liabilities of pledgees, agents and trustees.⁶⁶ The transferee of stock is liable for assessments.⁶⁷ Where a husband, without the knowledge or consent of his wife, caused shares of stock to be issued and entered on the books in her name, and she did not ratify the act, she was not liable to assessment; and ratification of the issuance and entry on the books of shares of stock in one's name, without her knowledge or consent, is not shown by her indorsement of the stock in blank to correct the supposed error, on being told by her husband who had caused the stock to be issued, that it was a mistake.⁶⁸

§ 4275. Mode of levying assessments; equality. Notice of an assessment given to the record holder of the stock is sufficient even though a third person has a joint interest in the stock.⁶⁹

§ 4276. Enforcement of assessments; forfeiture. The by-laws need not fix the place of sale of stock for failure to pay assessments.⁷⁰ Sale of stock for failure to pay assessments, on

⁶³ *Huxtable v. Berg*, 98 Wash. 616, 168 Pac. 187.

⁶⁴ *Devney v. Harriett State Bank*, — Minn. —, 177 N. W. 460.

⁶⁵ *Glenn v. California Trona Co.*, 38 Cal. App. 601, 177 Pac. 178.

⁶⁶ Duty of executor to pay assessments on stock, see *Hurlbert v. Title Insurance & Trust Co.*, — Cal. —, 186 Pac. 142.

⁶⁷ *Gaffney v. People's Trust Co.*, 191 N. Y. App. Div. 697, 182 N. Y. Supp. 451.

⁶⁸ *Williams v. Vreeland*, 250 U. S. 295, 63 L. Ed. 989, aff'g 244 Fed. 346.

⁶⁹ *Whitcomb v. Giannini*, — Cal. App. —, 184 Pac. 887.

⁷⁰ *Mitchell v. Blue Star Min. Co.*, 98 Wash. 191, 167 Pac. 130.

the street in front of the office building of the corporation, is not within a statute forbidding a sale "at the office of the company."⁷¹ Where a sale of stock for unpaid assessments is required, by statute, to be made for cash, the stock sold may be recovered where the price was paid by a promissory note, although such note was paid before the action was brought to recover the stock.⁷² An arrangement to refrain from competitive bidding at a sale of stock for assessments is inequitable, and equity will not permit parties to such a transaction to retain the fruits thereof.⁷³

The mere fact that one is a stockholder gives a foreign court no jurisdiction to render a judgment in personam against him for the amount assessed against him in the proceedings in the foreign court for winding up the company, where he did not appear and was not served with process.⁷⁴

§ 4277. Estoppel of stockholders; acquiescence. An original incorporator whose stock is nonassessable waives the right to claim such exemption by acquiescing in the enactment of a by-law making the stock assessable, and in the payment of several assessments.⁷⁵

§ 4278. Remedies in case of unauthorized or irregular assessments or forfeitures. Stockholders who pay invalid assessments may sue the corporation for a return of the money paid.⁷⁶ A transfer of shares of stock also transfers the right to participate in a refund of assessments paid, as agreed on when the assessments were paid, where that appears to have been the intention of all the parties.⁷⁷ A sale of stock for an illegal assessment may

⁷¹ Mitchell v. Blue Star Min. Co., 98 Wash. 191, 167 Pac. 130.

⁷² Newhall v. Hunsaker, 38 Cal. App. 399, 176 Pac. 380.

⁷³ Seymour v. Salsberry, — Cal. —, 171 Pac. 938.

⁷⁴ Traders' Trust Co. v. Davidson, — Minn. —, 178 N. W. 735.

⁷⁵ Jonas v. Frost, 32 Idaho 214, 179 Pac. 949.

⁷⁶ Huey v. Patterson, 37 Cal. App. 325, 174 Pac. 939.

⁷⁷ Cochrane v. Interstate Packing Co., 139 Minn. 452, 167 N. W. 111.

Construction of contract for refund of assessments paid on stock out of the "first net profits" of the company, see Cochrane v. Interstate Packing Co., 139 Minn. 452, 167 N. W. 111.

be enjoined.⁷⁸ Where stock is sold for nonpayment of an assessment, an action to set aside the sale because of irregularity must be brought within six months, under the California statutes.⁷⁹ Where a statute fixes a time within which an irregular or defective sale of stock for unpaid assessments may be avoided, it cannot be claimed that a stockholder is estopped by delaying to sue for less than such time.⁸⁰

In an action to set aside a sale of stock for unpaid assessments, statutes often require the plaintiff to pay or tender to the corporation, or to the party holding the stock sold, the sum for which the same was sold, where the sale is objected to because of irregularity or defects therein.⁸¹ The burden is on one attacking an assessment to show its invalidity.⁸²

§ 4279. Contracts that stock shall be nonassessable. Nonassessability of stock need not be evidenced by the certificates of stock but may be proved by any competent evidence.⁸³ A corporation is estopped to deny the recital in its certificates of stock that the stock was "fully paid and nonassessable," in mandamus to compel a transfer of stock on the books to a purchaser.⁸⁴

XXXVI. INDIVIDUAL LIABILITY AND RIGHTS ON FAILURE TO INCORPORATE

§ 4281. Liability to third persons generally. Where individuals act under a corporate form and in a corporate name, when in fact there is no corporation, they are individually liable as partners.⁸⁵ This applies where persons intending to

⁷⁸ First Nat. Bank v. Multnomah State Bank, 87 Ore. 423, 170 Pac. 534.

⁷⁹ Whitcomb v. Giannini, — Cal. App. —, 184 Pac. 887, holding that failure to give notice of meeting at which sale was postponed was a mere irregularity.

⁸⁰ Newhall v. Hunsaker, 38 Cal. App. 399, 176 Pac. 380.

⁸¹ See Glenn v. California Trona Co., 38 Cal. App. 601, 177 Pac. 178.

⁸² Glenn v. California Trona Co., 38 Cal. App. 601, 177 Pac. 178.

⁸³ Reinertsen v. Idaho Power & Concentrating Co., 32 Idaho 353, 182 Pac. 851.

⁸⁴ Hight v. Farmers' Grain Co., 214 Ill. App. 195.

⁸⁵ Pilsen Brewing Co. v. Wallace, 291 Ill. 59, 8 A. L. R. 579, 125 N. E. 714; Hall v. Robertson, 213 Ill. App. 147; Booth v. Scott, 276 Mo. 1, 205 S. W. 633, applying

form a corporation engage in business before carrying out or completing such intention.⁸⁶ So persons who transact business in the name of a foreign corporation not admitted to do business in the state are personally liable as partners.⁸⁷ The two owners of nearly all the stock are not personally liable, however, merely because they neglect to perform the ordinary corporate acts in the manner provided by law.⁸⁸ Merely filing a claim in bankruptcy against a pretended corporation is not a bar to an action against the stockholders as partners.⁸⁹ A person who has merely contracted for the purchase of stock, but to whom no stock has been transferred, cannot be held liable as a partner.⁹⁰

§ 4283. Members as partners inter se. Where persons do business under a corporate name but there is not even a de facto corporation, there is no estoppel as between themselves to deny a partnership although they may be liable to third persons as partners.⁹¹

rule to foreign corporation; Commerce Trust Co. v. McMechen, — Mo. App. —, 220 S. W. 1019; Pocahontas Fuel Co. v. Tarboro Cotton Factory, — N. C. —, 93 S. E. 790; Hill v. Turnverein Germania, — Okla. —, 187 Pac. 920. See also Breitzke v. Tucker, 129 Ark. 401, 196 S. W. 462.

⁸⁶ Commerce Trust Co. v. McMechen, — Mo. App. —, 220 S. W. 1019.

⁸⁷ Booth v. Scott, 276 Mo. 1, 205 S. W. 633.

⁸⁸ Morrison v. Griffin Corners Water Co., 190 N. Y. App. Div. 45, 179 N. Y. Supp. 333.

⁸⁹ Hall v. Robertson, 213 Ill. App. 147.

⁹⁰ Waseo Supply Co. v. Smith, 134 Ark. 23, 203 S. W. 6.

⁹¹ Lyons v. Van Oel, 183 Iowa 114, 165 N. W. 376.

CHAPTER 57

AMENDMENT OR REPEAL OF CHARTER

II. CONSTITUTIONAL LIMITATIONS ON AMENDMENT OR REPEAL

- § 4290. Charter of corporation as contract.
- § 4294. What constitutes an impairment of the obligations of contracts—
Of the contract between the corporation and its stockholders.
- § 4296. — Of the contracts of public service corporations.

III. RESERVATION OF POWER TO ALTER, AMEND OR REPEAL

- § 4299. In general.
- § 4300. Constitutional and statutory provisions—In general.
- § 4304. Effect of reservation of power upon legislative power.
- § 4308. Extent of reserved power—In general.
- § 4315. — Extent of reserved power to alter or amend—In general.
- § 4316. — — Constitutional restrictions.
- § 4319. — — Arbitrary and unreasonable amendments.

IV. PARTICULAR ALTERATIONS, AMENDMENTS AND REPEALS

- § 4334. Railroad companies.

V. MODE OF AMENDING CHARTERS

- § 4343. By corporations or their members.
- § 4344. Procedure, registration, fees, etc.

VI. ACCEPTANCE OF AMENDMENT

- § 4348. Form, evidence and presumption of acceptance.

VII. EFFECT OF AMENDMENT OR REPEAL

- § 4350. Amendment—Effect in general.
- § 4354. Estoppel and laches as to amendment and acceptance.

II. CONSTITUTIONAL LIMITATIONS ON AMENDMENT OR REPEAL

§ 4290. Charter of corporation as contract.¹ The charter of a corporation is an inviolable contract,² but all charters are subject to the police power.³

¹ For article on "Should the Dartmouth College Case be Recalled," see 51 Am. L. Rev. 711-751.

& H. River R. Co. v. Mealy, 224 N. Y. 187, 120 N. E. 155.

³ Waterbury v. Central Vermont R. Co., — Vt. —, 108 Atl. 423.

² People ex rel. New York Cent.

§ 4294. What constitutes an impairment of the obligations of contracts—Of the contract between the corporation and its stockholders. A voluntary amendment of a charter is void where it changes the fundamental arrangement and plans of the corporation, and violates contractual rights of stockholders to dividends.⁴

§ 4296. — Of the contracts of public service corporations. The state cannot, by contract with a charitable corporation, divest itself of the power to condemn property of such corporation for streets or the like.⁵ The business of a company operating only on private property and manufacturing electricity only for itself and tenants is not “of the same general character” as that of a public service corporation, so as to authorize an amendment of the charter to transform it into an electric light corporation.⁶ Where a railroad company, by its charter, is given the right to own and operate a railroad in the state, and to do an intrastate business therein, the state cannot violate such charter rights by the exercise of mere assumed police power.⁷

III. RESERVATION OF POWER TO ALTER, AMEND OR REPEAL

§ 4299. In general. In Canada, parliament reserves the power to repeal or amend charters.⁸

§ 4300. Constitutional and statutory provisions—In general. The power to change or repeal a charter is sometimes reserved by the statute authorizing the creation of certain corporations.⁹

§ 4304. Effect of reservation of power upon legislative power. If the state reserves the power to amend or repeal, a subsequent

⁴ *Allen v. White*, 103 Neb. 256, 171 N. W. 52.

⁵ *Pennsylvania Hospital v. Philadelphia*, 245 U. S. 20, 62 L. Ed. 124, aff'g 254 Pa. 392, 98 Atl. 1077.

⁶ *People ex rel. Cayuga Power Corporation v. Public Service Commission*, 226 N. Y. 527, 124 N. E. 105, rev'g 184 N. Y. App. Div. 781, 172 N. Y. Supp. 533.

⁷ *State ex rel. Wabash R. Co. v. Roach*, 267 Mo. 300, 184 S. W. 969.

⁸ *McClement v. Supreme Court I. O. F.*, 222 N. Y. 470, 119 N. E. 99.

⁹ *Integrity Mut. Ins. Co. v. Boys*, 293 Ill. 307, 127 N. E. 748.

exercise of such power does not impair the obligations of the contract.¹⁰

§ 4308. **Extent of reserved power—In general.**¹¹ Where the state reserves the right to amend or repeal the charter, a railroad company granted street rights by a municipality cannot complain of the occupancy by an electric light company of a highway crossing the railroad tracks where none of the poles are on the right of way and the wires are thirty feet above the rails.¹²

§ 4315. — **Extent of reserved power to alter or amend—In general.** Where power of the state to amend the charter exists, reasonable restrictions may be imposed on the transaction of business, such as requiring a license of milk dealers.¹³

§ 4316. — **Constitutional restrictions.** Vested rights cannot be taken away by amendment of the charter; but vested rights are not taken away by increasing the amount of the assessments agreed upon by a fraternal benefit society, where the contract of insurance or the charter provide that the assessments may be changed from time to time.¹⁴

§ 4319. — **Arbitrary and unreasonable amendments.** Reserving the right to amend a charter does not authorize a deprivation of benefits, or impairment of the value of the franchise by imposing additional burdens, without compensation.¹⁵

IV. PARTICULAR ALTERATIONS, AMENDMENTS AND REPEALS

§ 4334. **Railroad companies.** Reservation by the state of the right to repeal or amend a railroad charter does not authorize a requirement that the company carry state officials free of charge.¹⁶

¹⁰ *Sears v. City of Akron*, 246 U. S. 242, 62 L. Ed. 688.

¹¹ See also § 4296, *supra*.

¹² *New York Cent. R. Co. v. Middleport Gas & Electric Light Co.*, 193 N. Y. App. Div. 273, 184 N. Y. Supp. 221.

¹³ *People v. Beakes Dairy Co.*, 222 N. Y. 416, 119 N. E. 115.

¹⁴ *McClement v. Supreme Court I. O. F.*, 222 N. Y. 470, 119 N. E. 99.

¹⁵ *People v. International Bridge Co.*, 223 N. Y. 137, 119 N. E. 351.

¹⁶ *Napier v. Delaware, L. & W. R. Co.*, 91 N. J. L. 282, 102 Atl. 444.

V. MODE OF AMENDING CHARTERS

§ 4343. By corporations or their members. A corporation may adopt as an amendment of its charter a provision which could have been inserted in the original articles of incorporation.¹⁷ The mere fact that a paper is denominated "amended articles of incorporation" does not make it such unless executed in pursuance to the statute.¹⁸ The secretary of state cannot refuse to file a certificate whereby a corporation seeks to be bound by and come within a certain statute, on the ground the statute permitting corporations to so change the nature of the corporation is unconstitutional as impairing the obligation of contracts as to stockholders, since he is not an interested party.¹⁹

§ 4344. Procedure, registration, fees, etc.²⁰

VI. ACCEPTANCE OF AMENDMENT

§ 4348. Form, evidence and presumption of acceptance. An amendment may become a part of the charter of an existing corporation without formal adoption, in a proper case.²¹

VII. EFFECT OF AMENDMENT OR REPEAL

§ 4350. Amendment—Effect in general. A charter amendment to provide for an increase of stock does not affect the identity of the company.²²

§ 4354. Estoppel and laches as to amendment and acceptance. The fact that an amendment of corporate articles was not legally adopted cannot be urged by parties in interest after acquiescence therein for seventeen years.²³

¹⁷ Pyle v. National Life Ass'n of Des Moines, 186 Iowa 756, 172 N. W. 944.

¹⁸ Western Casualty & Guaranty Ins. Co. v. Capitol State Bank of Oklahoma City, — Okla. —, 172 Pac. 954.

¹⁹ Mohall Farmers' Elevator Co. v. Hall, — N. D. —, 176 N. W. 131.

²⁰ Fees, see § 225, supra.

²¹ Atlanta Loan & Saving Co. v. Norton, 149 Ga. 805, 102 S. E. 536, citing Fletcher Cyc. Corp. § 784.

²² Wright v. Barnard, 248 Fed. 756, 775.

²³ Chicago, M. & St. P. R. Co. v. Des Moines Union R. Co., 254 Fed. 927.

CHAPTER 58

GOVERNMENTAL CONTROL OF CORPORATIONS

I. GENERAL CONSIDERATIONS

§ 4365. Police power as applicable to corporations—Grant of special franchise to use streets or contract as affecting police power.

II. WHO MAY EXERCISE THE POWER

§ 4367. In general.

§ 4368. Federal government.

§ 4370. State legislature—In general.

§ 4371. — State control over corporations created by Congress.

§ 4374. Municipalities.

III. CORPORATIONS SUBJECT TO REGULATION

§ 4377. Corporations whose business is affected with a public interest—Insurance companies.

§ 4379. Corporations subject to jurisdiction of public service commissions.

IV. PUBLIC SERVICE COMMISSIONS

§ 4381. Constitutionality of delegation of power.

§ 4383. Nature of powers of commissions.

§ 4384. Extent and scope of powers of commissions—In general.

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V. REGULATIONS AS VIOLATIONS OF FEDERAL CONSTITUTION

§ 4392. Interference with interstate commerce—In general.

§ 4393. — Illustrations of rules.

§ 4394. Impairment of contract—In general.

§ 4395. — Power to revoke or burden franchises.

§ 4398. Due process of law—Unreasonable regulations.

§ 4399. — Impairment of franchise.

§ 4404. Denial of equal protection of the laws—Regulations applicable only to corporations.

§ 4405. — Regulations applicable only to certain class of corporations.

§ 4406. — Regulations applicable only to certain corporations of a particular class.

§ 4407. — Regulations of common carriers.

§ 4408. — Regulations of railroad companies.

- § 4411. — Regulations of telegraph companies.
- § 4416. Regulations prohibiting the granting of special privileges or immunities.

VI. PARTICULAR REGULATIONS OTHER THAN THOSE RELATING TO RATES

- § 4417. General considerations.
- § 4418. Requiring certificate of public convenience and necessity.
- § 4420. Requiring consent of commission to transfer of property of public service corporation or consolidation of corporations.
- § 4421. "Blue Sky" laws.
- § 4423. Regulations to prevent corporations withdrawing, wholly or in part, from public service.
- § 4425. Regulations imposing penalties—In general.
- § 4427. — Unreasonable penalties.
- § 4428. Regulations as to employees.
- § 4429. — Amount of wages.
- § 4433. License fees—Where right to use streets has been granted by federal government or by state.
- § 4434. — Reasonableness of amount of license.
- § 4435. — Application of rules to particular corporations.
- § 4436. Regulations of railroad companies—In general.
- § 4437. — Requiring extension of line.
- § 4438. — Requiring operation of road or of trains.
- § 4439. — Requiring stopping of trains at stations.
- § 4440. — Regulations as to depots.
- § 4441. — Regulating running time of trains.
- § 4442. — Requiring connections with other roads.
- § 4443. — Requiring construction of spur tracks.
- § 4444. — Regulations as to grade crossings.
- § 4445. — Requiring lighting of tracks.
- § 4446. — Regulating rate of speed.
- § 4448. — Requiring signals or flagmen.
- § 4450. — Requiring fencing of tracks and building of cattle guards.
- § 4451. — Regulations as to sleeping car service.
- § 4452. Regulations of street railroad companies.
- § 4453. Regulations of telegraph, telephone and electric light companies—
In general.
- § 4454. — Regulations as to poles and wires.
- § 4455. — Requiring wires to be put underground.
- § 4456. — Requiring physical connection of lines.
- § 4457. Regulation of gas companies.
- § 4461. Regulation of mining companies.

VII. REGULATION OF RATES

A. Right to Regulate and General Considerations

- § 4468. Power to require and regulate street car transfers.
- § 4469. Power as extending to increasing as well as reducing rates.

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- § 4470. Particular companies whose rates may be regulated.
- § 4471. Rates of municipal plants.
- § 4473. Fixing rates by contract as distinguished from "regulation" of rates independently of agreement—Power of municipality to "contract" as to rates.
- § 4474. —Company as precluded from denying power to contract or reasonableness of rates.
- § 4475. Penalties for violation of rate laws.

B. Who May Regulate Rates

- § 4477. United States.
- § 4478. State.
- § 4479. Public service commission.
- § 4480. Municipal corporation—In general.
- § 4482. —Particular delegations of power.
- § 4483. —Regulating rates outside municipality.
- § 4484. Courts.

C. Regulation of Rates as Violating Constitutional Provisions

- § 4485. Interference with interstate commerce.
- § 4486. Due process of law.
- § 4487. Denial of equal protection of the laws.
- § 4488. Impairment of obligation of contract—In general.
- § 4490. —As dependent upon power of municipality to make contract as to rates.
- § 4493. —Franchise as constituting an actual contract as to rates.
- § 4494. —Power of municipality to change rate as distinguished from power of state.
- § 4495. —Right of corporation or commission to increase rates.
- § 4496. —Regulations as impairing contracts between corporation and third person.
- § 4497. —Waiver or abandonment of contract rights.

D. Discrimination in Rates

- § 4498. General considerations.
- § 4507. Free or reduced rates for particular passengers—Six tickets for a quarter.
- § 4512. —Requiring reduced or free transportation for soldiers, police officers, detectives, etc.
- § 4513. —Forbidding issuance of free passes.

E. Reasonableness of Rates Fixed by Law

- § 4517. General rules.
- § 4518. Matters to be considered.
- § 4526. Reasonableness of return as a whole.
- § 4527. Reasonableness as affected by comparison with rates of other companies or in other localities.

- § 4529. Methods of valuation in general.
- § 4530. Original cost as test.
- § 4531. Present value as test—General rule.
- § 4532. — What constitutes “value” in general.
- § 4535. — Value of property not used.
- § 4537. — Value as “going concern” as item.
- § 4538. — Franchise as item of value.
- § 4539. — Good will as item of value.
- § 4541. — Deduction for depreciation.
- § 4543. Cost of reproduction **as test—In general.**
- § 4546. Operating expenses—In general.
- § 4547. — Depreciation fund.
- § 4548. Rate of return to which corporation entitled.

VIII. PROCEDURE CONNECTED WITH REGULATIONS AND REVIEW THEREOF

- § 4551. Procedure before commission—In general.
- § 4552. — Notice and hearing.
- § 4558. Review by courts in general—Power to review.
- § 4559. — Compliance with conditions precedent.
- § 4560. — Presumptions and burden of proof.
- § 4562. — Scope of review and grounds for attack.
- § 4564. — Who may attack.
- § 4566. Particular methods of review—Injunction suits.
- § 4568. — Appeals.
- § 4572. Proceedings maintainable by individual consumer or patron.

I. GENERAL CONSIDERATIONS

§ 4365. Police power as applicable to corporations—Grant of special franchise to use streets or contract as affecting police power. A franchise, even though a contract which cannot be impaired, is subject to the police power of the state.¹ After a street franchise has expired, but the company continues to use the streets, the city may regulate such use subject to the condition that it must not bring about confiscation.²

II. WHO MAY EXERCISE THE POWER

§ 4367. In general. There is no general visiting power in the courts unless conferred by statute.³

¹ Central Union Telephone Co. v. Indianapolis Telephone Co., — Ind. —, 126 N. E. 628.

state. Southwest Missouri R. Co. v. Public Service Commission, — Mo. —, 219 S. W. 380.

Conditions imposed by a city in granting a street franchise to a street car company are no limitation on the police power of the

² City of Toledo v. Toledo Railways & Light Co., 259 Fed. 450.

³ In re Norton, 97 N. Y. Misc. 289, 161 N. Y. Supp. 710.

§ 4368. Federal government.⁴§ 4370. State legislature—In general.⁵

§ 4371. — **State control over corporations created by Congress.**⁶ A state has power over companies operating bridges between states, where Congress has not acted;⁷ but a state cannot regulate relief associations of interstate carriers, by forbidding waiver of damages on the part of employees, since regulated by act of Congress.⁸ State control of a bridge company owning an international bridge is not lost because of an act of congress requiring consent of Congress to a bridge across international waters.⁹

§ 4374. **Municipalities.** Where a street railway is using city streets without a franchise, the city may eject it or prescribe reasonable conditions.¹⁰

III. CORPORATIONS SUBJECT TO REGULATION

§ 4377. **Corporations whose business is affected with a public interest—Insurance companies.** The business of insurance is clothed with a public interest so as to be subject to regulation.¹¹ Insurance companies are among those which the state may regu-

⁴ The next step in the national control of corporations is the subject of an article by Mr. J. H. Wilkerson in 90 Cent. L. J. 113-124.

⁵ Power of legislature to investigate conduct of private person, corporation or institution, see note in 9 A. L. R. 1341, annotating *Greenfield v. Russell*, 292 Ill. 392, 9 A. L. R. 1334, 127 N. E. 102.

⁶ See also §§ 4392, 4393, 4485, *infra*.

⁷ *Proprietors of Cornish Bridge v. Fitts*, — N. H. —, 107 Atl. 626.

Interstate bridges are not subject to control by the states except to a very limited extent.

Shrader v. Steubenville, E. L. & B. Val. Traction Co., — W. Va. —, 99 S. E. 207.

⁸ *Pittsburgh, C., C. & St. L. R. Co. v. Miller*, 187 Ind. 684, 120 N. E. 706; — Ind. —, 119 N. E. 801.

⁹ *International Bridge Co. v. People of State of New York*, 254 U. S. 126, 65 L. Ed. —, *aff'g* 223 N. Y. 137, 119 N. E. 351.

¹⁰ *Henry L. Doherty & Co. v. Toledo Railways & Light Co.*, 254 Fed. 597.

¹¹ *La Tourette v. McMaster*, 248 U. S. 465, 63 L. Ed. 362; *Lewelling v. Manufacturing Wood-Workers' Underwriters*, 140 Ark. 124, 215 S. W. 258.

late by requiring mutual insurance companies to have a certain surplus.¹²

§ 4379. Corporations subject to jurisdiction of public service commissions.¹³ A corporation is not a "public utility" and subject to regulation as such by a public service commission, merely because of the existence of certain charter power, where such power has never been exercised.¹⁴ The following have been held to be "public utilities," so as to be subject to regulation by state public service commissions: a pipe line company carrying oil for all producers;¹⁵ a canal company which delivers water for agricultural and other purposes.¹⁶

The following have been held not public utilities subject to such regulation: a corporation manufacturing electricity only for itself and tenants;¹⁷ a brewery company which sells surplus electricity to individuals in the vicinity through a subsidiary company;¹⁸ a land company furnishing water for irrigation to purchasers of land;¹⁹ an irrigation company with charter power to sell water to the public, where in fact it has never sold water except to purchasers of land from it in fulfilment of private contracts.²⁰

IV. PUBLIC SERVICE COMMISSIONS

§ 4381. Constitutionality of delegation of power. The Illinois Public Utilities Act is a valid exercise of the police power.²¹

¹² Integrity Mut. Ins. Co. v. Boys, 293 Ill. 307, 127 N. E. 748.

¹³ What are quasi public corporations in general, see § 73, supra.

¹⁴ De Pauw University v. Public Service Commission, 253 Fed. 848.

¹⁵ Producers Transp. Co. v. Railroad Commission, 251 U. S. 228, 64 L. Ed. 239, aff'g 176 Cal. 499, 169 Pac. 59.

¹⁶ Steamboat Canal Co. v. Garson, — Nev. —, 185 Pac. 801.

¹⁷ People ex rel. Cayuga Power Corporation v. Public Service Commission, 226 N. Y. 527, 124 N. E. 105, rev'g 184 N. Y. App.

Div. 781, 172 N. Y. Supp. 533.

¹⁸ State v. Public Service Commission, 275 Mo. 483, 205 S. W. 36.

¹⁹ De Pauw University v. Public Service Commission, 247 Fed. 183.

²⁰ De Pauw University v. Public Service Commission, 253 Fed. 848, Oregon statute.

The fact that notice of appropriation of water states that it is for "general rental, sale," etc., does not necessarily make the appropriating corporation a public utility. De Pauw University v. Public Service Commission, 253 Fed. 848.

²¹ Schiller Piano Co. v. Illinois

§ 4383. **Nature of powers of commissions.** An order of a commission fixing maximum future rates is legislative in character.²²

§ 4384. **Extent and scope of powers of commissions—In general.** The supervisory powers of a state corporation commission over insurance companies is wholly statutory and it has no implied powers except those actually necessary to carry out the express powers.²³

§ 4385. — **Powers of state commission over interstate railroads.**²⁴

V. REGULATIONS AS VIOLATIONS OF FEDERAL CONSTITUTION

§ 4392. **Interference with interstate commerce—In general.** Piping of natural gas from one state to another is interstate commerce.²⁵

§ 4393. — **Illustrations of rules.** A state may provide for inspection of oils and gasoline, while yet in interstate transit, and impose a charge upon the oil company reasonably sufficient to cover the cost of inspection.²⁶ A city may obtain a temporary injunction restraining discontinuance of gas supply although property in another state where the gas wells are located will be affected.²⁷ The transmission of interstate messages by telegraph companies, being interstate commerce and expressly put under the control of the Interstate Commerce Commission, is not subject to state regulation.²⁸ A separate coach law for

Northern Utilities Co., 288 Ill. 580, 123 N. E. 631.

²² Ohio Valley Water Co. v. Ben Avon Borough, 253 U. S. 287, 64 L. Ed. 908, rev'g on other grounds 260 Pa. 289, 103 Atl. 744.

²³ Johnson v. Betts, — Ariz. —, 188 Pac. 271.

²⁴ See § 4485, *infra*.

²⁵ Landon v. Public Utilities Commission, 245 Fed. 950; People ex rel. Pennsylvania Gas Co. v.

Saxe, — N. Y. —, 128 N. E. 673, rev'g 186 N. Y. App. Div. 28, 174 N. Y. Supp. 102.

²⁶ Pure Oil Co. v. State of Minnesota, 248 U. S. 158, 63 L. Ed. 180, aff'g 134 Minn. 101, 158 N. W. 753.

²⁷ City of Jamestown v. Pennsylvania Gas Co., 264 Fed. 1009.

²⁸ Western U. Tel. Co. v. Hamilton, — Ind. App. —, 125 N. E. 45; Leftridge v. Western U. Tel.

white and colored passengers does not interfere with interstate commerce as applied to a road wholly in the state, although operated by a domestic corporation whose lines extend into another state and which carries passengers over such road to the other state for a single fare.²⁹ A regulation by the state of grain elevators and cars therefor, where interfering with interstate commerce of the railroad, is invalid.³⁰

A state cannot forfeit the charter of a domestic corporation authorized to build a bridge for interstate commerce, by requiring construction of the bridge in five years, where Congress has granted the company a franchise.³¹ Congress having declared lawful a bridge proposed to be erected and having authorized its erection, no authority remains in the state to make any new or other regulations or requirements, the bridge being over navigable waters for interstate commerce.³²

Transmission of stock quotations on the New York Stock Exchange, pursuant to a contract between it and a telegraph company and subscribers to the service, is interstate commerce until completed in the subscribers' offices, so as to prevent regulation by a state requiring cessation of alleged discriminations.³³

§ 4394. Impairment of contract—In general.³⁴ A proper exercise of the police power does not impair the obligation of a

Co., 277 Mo. 90, 210 S. W. 18; Western U. Tel. Co. v. Bowles, 124 Va. 730, 98 S. E. 645.

State control of interstate telegraph companies, see also Speight v. Western U. Tel. Co., 178 N. C. 146, 100 S. E. 351.

²⁹ South Covington & C. St. R. Co. v. Com., 252 U. S. 399, 64 L. Ed. 631, aff'g 181 Ky. 449, 205 S. W. 603.

³⁰ Chicago, R. I. & P. R. Co. v. State, — Okla. —, 180 Pac. 246.

³¹ People v. Hudson River Connecting R. Co., 228 N. Y. 203, 126 N. E. 801.

³² People v. Hudson River Connecting R. Corporation, 228 N. Y. 203, 126 N. E. 801. Same case,

see 186 N. Y. App. Div. 602, 174 N. Y. Supp. 754.

³³ Western U. Tel. Co. v. Foster, 247 U. S. 105, 62 L. Ed. 1006, 1 A. L. R. 1278, rev'g 224 Mass. 365, 113 N. E. 192.

³⁴ For note on "Privilege of using street as a contract within the constitutional provision against impairing the obligation of contracts," see L. R. A. 1918 E 892.

Note on "Examination and supervision of banks by public officers as impairment of charter rights," see 8 A. L. R. 898, annotating Bank of Oxford v. Love, 111 Miss. 699, 8 A. L. R. 894, 72 So. 133.

contract.³⁵ A bank charter conferring control on its stockholders pursuant to such rules as they may adopt, does not preclude, as impairing the contract, a statute providing for examination of the bank and imposing a reasonable annual assessment for the maintenance of the state banking department.³⁶ Contracts of telegraph companies to furnish franks in return for a grant of a right of way cannot be impaired by state legislation, so far as intrastate messages are concerned.³⁷

§ 4395. — Power to revoke or burden franchises. A municipal franchise is a contract the obligations of which cannot be impaired.³⁸ In Iowa, however, all franchises are, by statute, subject to change by the state.³⁹

There is no contract where town officers, imposing conditions as to maintaining a bridge, on granting a location to a street railway company, act as public officers exercising a governmental function for the safety of the public, and not as agents of the town.⁴⁰

No impairment of contract forbidden by the Federal Constitution is involved where the only issue is as to whether a city or the public service commission is authorized to exercise the governmental power to regulate rates subject to which a franchise was granted.⁴¹ Exemption by municipal contract, of a railroad company, from street pavement assessments, cannot be impaired by subsequent legislation.⁴²

³⁵ Schiller Piano Co. v. Illinois Northern Utilities Co., 288 Ill. 580, 123 N. E. 631.

³⁶ Bank of Oxford v. Love, 250 U. S. 603, 63 L. Ed. 1165, aff'g 111 Miss. 699, 8 A. L. R. 894, 72 So. 133.

³⁷ Irvine v. Postal Telegraph-Cable Co., 37 Cal. App. 60, 173 Pac. 487.

³⁸ Michigan Ry. Co. v. Lansing, 260 Fed. 322; Sullivan v. Best, 286 Ill. 315, 121 N. E. 565; Vincennes v. Vincennes Traction Co., — Ind. —, 120 N. E. 27; Kennon v. Hilburn, 144 La. 131, 80 So. 225.

Street franchises in Ohio are contracts not subject to revocation during their life. Northern Ohio

Traction & Light Co. v. State of Ohio ex rel. Pontius, 245 U. S. 574, 62 L. Ed. 481, L. R. A. 1918 E 865, rev'g 93 Ohio St. 466, 114 N. E. 53.

³⁹ Burlington Railway & Light Co. v. Burlington, — Iowa —, 176 N. W. 285; Selkirk v. Sioux City Gas & Electric Co., — Iowa —, 176 N. W. 301.

⁴⁰ In re Knox County Elec. Co., — Me. —, 109 Atl. 898.

⁴¹ City of Pawhuska v. Pawhuska Oil & Gas Co., 250 U. S. 394, 63 L. Ed. 1054, dismissing writ of error to review — Okla. —, 166 Pac. 1058.

⁴² City Council of Augusta v. Augusta-Aiken Railway & Electric

§ 4398. Due process of law—Unreasonable regulations.⁴³

§ 4399. — Impairment of franchise. Where there is nothing in a contract between public utility corporations which is injurious to public welfare, the contract cannot be deemed terminated by virtue of the Public Utilities Act, since to do so would constitute a taking of property without due process of law.⁴⁴

§ 4404. Denial of equal protection of the laws—Regulations applicable only to corporations. A statute providing for recovery of an attorney's fee in actions against corporations is unconstitutional where not applicable to actions against partnerships and individuals.⁴⁵ A statute authorizing libel suits against corporations to be brought in the county where plaintiff resides denies the equal protection of the laws to corporations, where individuals can be sued for libel only in the county in which they are found.⁴⁶ A statute imposing penalties on light and gas companies for failure to furnish gas and electricity was held constitutional although not including individuals or partnerships, on the theory that public lighting was practically always conducted by a corporation.⁴⁷

§ 4405. — Regulations applicable only to certain class of corporations.⁴⁸ Public service corporations may be put in a class by themselves and required to give service letters to employees discharged or leaving the service;⁴⁹ and they may be separately classified as to the date when compensation shall be assessed in condemnation proceedings.⁵⁰ But public service cor-

Co., — Ga. —, 104 S. E. 503.

⁴³ What regulations are reasonable, see § 4436 et seq., *infra*.

⁴⁴ *Schiller Piano Co. v. Illinois Northern Utilities Co.*, 288 Ill. 580, 123 N. E. 631.

⁴⁵ *Anderson v. Uncle Sam Oil Co.*, 106 Kan. 483, 186 Pac. 198.

⁴⁶ *McClung v. Pulitzer Pub. Co.*, 279 Mo. 370, 214 S. W. 193.

⁴⁷ *Hansen v. Vallejo Elec. Light*

& Power Co., — Cal. —, 188 Pac. 999.

⁴⁸ Usury statutes as denying equal protection of the laws because of exclusion of certain corporations, see *People v. Stokes*, 281 Ill. 159, 118 N. E. 87.

⁴⁹ *Dickinson v. Perry*, 75 Okla. 25, 181 Pac. 504.

⁵⁰ *Marin Municipal Water Dist. v. Marin Water & Power Co.*, 178 Cal. 308, 173 Pac. 469.

porations are denied the equal protection of the laws where the defense of fellow-servants and assumption of risk are abolished as to them but not as to other private corporations.⁵¹ A statute providing for escheats of deposits after certain periods is not obnoxious as special legislation because applicable only to state corporations as distinguished from national, nor because it excludes mutual savings funds associations having no shares of capital stock, and building and loan associations.⁵² A statute requiring licenses from corporations organized to redeem trading stamps but not from corporations redeeming in articles of their own manufacture violates the equal protection of the law's clause.⁵³

§ 4406. — Regulations applicable only to certain corporations of a particular class.⁵⁴ There is no denial of equal protection of the laws in including land of a cemetery association in an assessment district, because other cemeteries have been districted separately for such purposes, where similarity of situation and conditions is not shown.⁵⁵ A water company is not denied equal protection of the laws because a statute permits a city to construct a rival plant but prohibits the city from extending its system in another direction into territory in which other companies are operating.⁵⁶

§ 4407. — Regulations of common carriers.⁵⁷

§ 4408. — Regulations of railroad companies. A statute making railroads liable to employees for acts of fellow-servants is not unconstitutional because not made applicable to other corporations.⁵⁸ Excluding steam railroads from statutory regulation of other public utilities as to carrying a depreciation account, mode of keeping records, necessity for obtaining leave

⁵¹ *Mason v. New Orleans Terminal Co.*, 143 La. 616, 79 So. 26.

⁵² *Germantown Trust Co. v. Powell*, 265 Pa. 71, 108 Atl. 441.

⁵³ *Sperry & Hutchinson Co. v. State*, 188 Ind. 173, 122 N. E. 584.

⁵⁴ See also § 4405, *supra*.

⁵⁵ *Mount St. Mary's Cemetery*

Ass'n v. Mullins, 248 U. S. 501, 63 L. Ed. 384, *aff'g* 268 Mo. 691, 187 S. W. 1169.

⁵⁶ *Norfolk County Water Co. v. Norfolk*, 246 Fed. 650.

⁵⁷ See § 4405, *supra*.

⁵⁸ *Seamer v. Great Northern R. Co.*, 142 Minn. 376, 172 N. W. 765.

to issue stock, bonds, etc., is not objectionable as class legislation.⁵⁹ Where other railroads are subject to the same obstruction of traffic by overflow, the state cannot arbitrarily select a particular road and require it to elevate its tracks at a certain place without requiring other roads to do so.⁶⁰

§ 4411. — Regulations of telegraph companies. Failure to enforce a license tax on poles in streets against other corporations in the same manner it was proposed to enforce the ordinance against a telegraph company does not show a violation of the equal protection clause of the Federal Constitution.⁶¹

§ 4416. Regulations prohibiting the granting of special privileges or immunities. An act is not unconstitutional as conferring special privileges on corporations because it authorizes licenses to corporations to arm employees, so as not to be subject to the charge of carrying concealed weapons.⁶²

VI. PARTICULAR REGULATIONS OTHER THAN THOSE RELATING TO RATES

§ 4417. General considerations. Attorney fee statutes are constitutional although retroactive.⁶³ The Ohio statute prohibiting corporations from compelling employees to join any association or holding out dues or waiving right to damages against railroad company for personal injury or death, is a valid police regulation, does not infringe the freedom of contract, and is not inconsistent with the Federal Employers' Liability Act.⁶⁴ One public service company cannot be made to supply a competitor with material necessary to enable it to discharge its duty to the public.⁶⁵

⁵⁹ *City of Memphis v. Enloe*, 141 Tenn. 618, 214 S. W. 71.

⁶⁰ *Hines v. Clarendon Levee Dist.*, 264 Fed. 127.

⁶¹ *Mackay Telegraph & Cable Co. v. City of Little Rock*, 250 U. S. 94, 63 L. Ed. 863, aff'g 131 Ark. 306, 199 S. W. 90.

⁶² *People v. Gogak*, 205 Mich. 260, 171 N. W. 428.

⁶³ *Germania Fire Ins. Co. v. Bally*, 19 Ariz. 580, 173 Pac. 1052.

⁶⁴ *Baltimore & O. S. W. R. Co. v. Bailey*, 99 Ohio St. 312, 124 N. E. 195.

⁶⁵ *Salisbury & S. Ry. Co. v. Southern Power Co.*, — N. C. —, 102 S. E. 625.

§ 4418. Requiring certificate of public convenience and necessity.⁶⁶ The Minnesota statute requiring the granting of a certificate by a commission, based on a reasonable public demand for a bank, as a condition of the right to engage in banking, is a proper exercise of the police power.⁶⁷ A statute prohibiting licensing public utilities for duplication of service, in the absence of certificates of public necessity therefor, does not create a monopoly, nor is it otherwise unconstitutional.⁶⁸

§ 4420. Requiring consent of commission to transfer of property of public service corporation or consolidation of corporations. The state has power to withdraw at any time power delegated to a city and confer it on a state public service commission; and where it has done so neither the city nor its inhabitants can complain that a telephone company sold its property without first obtaining the consent of the city as required by the franchise, where such right to consent had been withdrawn by the state from the city.⁶⁹

§ 4421. "Blue Sky" laws.⁷⁰ The purpose of Blue Sky laws is to protect the public against imposition, and they are a proper exercise of police power.⁷¹ The courts refuse to lay down a hard and fast rule by which to determine whether that which

⁶⁶ Issuing certificate of necessity to electric light company where another company is furnishing light in the locality, see *State ex rel. Electric Co. v. Atkinson*, 275 Mo. 325, 204 S. W. 897. Reasonableness of granting certificate of necessity and convenience to one of competing lines of motor busses, see *Chicago Motor Bus Co. v. Chicago Stage Co.*, 287 Ill. 320, 122 N. E. 477.

⁶⁷ *State ex rel. Dybdal v. State Securities Commission*, 145 Minn. 221, 176 N. W. 759.

⁶⁸ *Farmers' & Merchants' Co.-Op. Tel. Co. v. Boswell Tel. Co.*, 187 Ind. 371, 119 N. E. 513.

⁶⁹ *Central Union Telephone Co. v. Indianapolis Telephone Co.*, — Ind. —, 126 N. E. 628.

⁷⁰ See also §§ 520, 520a, 568, 3861, as to construction of act.

Consent to issuance of stock, construction of Blue Sky laws, see § 3477, *supra*.

Article on new Blue Sky Law in Illinois, see 14 Illinois Law Review 356, 367-377 by Mr. William Browne Hale.

⁷¹ *State v. Gopher Tire & Rubber Co.*, — Minn. —, 177 N. W. 937.

In Alberta, Canada, the Blue Sky Law applies to agreements to sell stock as well as to completed sales in companies not yet incorporated, and to foreign as well as domestic companies. *Rex v. Malcolm*, 42 Dom. L. Rep. (Can.) 90.

is offered to a prospective investor is such a "security" as may not be sold without a license.⁷²

In Michigan a foreign corporation cannot sell stock in the state without first securing permission from the Michigan Securities Commission. Construing the statute, it is held (1) that a person selling his own stock as an isolated act is not a "dealer"; (2) that an exchange of stock for that of other companies is a "sale" within the meaning of the statute; (3) that a sale in violation of the statute is void; (4) that on rescission the subscriber is entitled to be restored to what he has parted with; (5) that the subscriber is not estopped to rescind because of the execution of a proxy after the institution of the action to rescind.⁷³ In that state, a sale of stock by the owner is not within the Blue Sky Law since the seller in such a case is not a "dealer."⁷⁴ The Michigan Blue Sky Law was construed as to whether a person suing for commissions on sales of stock was a "dealer" or an "agent" within the meaning of the Blue Sky Law. The corporation sought to escape payment of commissions on the ground that plaintiff was a "dealer" and therefore not entitled to recover because of failure to file a broker's certificate, but the court held that he was an "agent" so that the corporation was required to pay his registration fee and could not set up its failure to do so as a defense.⁷⁵

In Minnesota, the offense of selling securities without a license, in violation of the Blue Sky Law, is not committed where there is only a single or isolated sale.⁷⁶ "Investment contracts,"

⁷² *State v. Gopher Tire & Rubber Co.*, — Minn. —, 177 N. W. 937.

⁷³ *Edward v. Ioor*, 205 Mich. 617, 172 N. W. 620.

The transfer of stock in a holding company for stock in controlled companies is a "sale" of stock within the Michigan Blue Sky Law. *Edward v. Ioor*, 205 Mich. 617, 172 N. W. 620.

⁷⁴ *Dows v. Schuh*, 206 Mich. 133, 172 N. W. 418; *Edward v. Ioor*, 205 Mich. 617, 172 N. W. 620.

A sale of stock by a stockholder of his own stock, some of which

stands in the name of members of his family, does not make him a "dealer" within the Blue Sky Law. *Dursum v. Benedict*, 209 Mich. 115, 176 N. W. 459.

⁷⁵ *Lovering v. Duplex Power Car Co.*, 204 Mich. 658, 171 N. W. 374.

⁷⁶ *State v. Gopher Tire & Rubber Co.*, — Minn. —, 177 N. W. 937.

Sufficiency of indictment, under Blue Sky Law, for selling securities without a license, see *State v. Gopher Tire & Rubber Co.*, — Minn. —, 177 N. W. 937.

within the meaning of its Blue Sky Law, includes certificates issued in consideration of cash and services, entitling the holder to share in the profits of the business.⁷⁷ A corporation issuing and selling certificates which provide that, in consideration of a sum paid by the purchaser and his assistance in promoting the sale of goods manufactured by the company, he shall share in the profits of the business, is engaged in the business of "selling securities" within the meaning of the Minnesota Blue Sky Law.⁷⁸ In Nebraska, the Blue Sky Law of 1913 was repealed and a new law substituted in 1919; and under the 1913 statute the question whether a particular corporation was exempted as having been in existence for a year before the statute was enacted, although decided in the particular case, is now not a litigious question under the 1919 law.⁷⁹ In North Dakota, a certificate for one hundred dollars to be issued by a corporation to be organized in the future to develop coal mines is a "speculative security" within the Blue Sky Law.⁸⁰

§ 4423. Regulations to prevent corporations withdrawing, wholly or in part, from public service.⁸¹ The state cannot compel a public utility to operate at a loss where it is willing to abandon all its property to the public.⁸²

A street car franchise for a certain number of years does not imply an absolute obligation to continue operation for such period.⁸³ If its franchise is permissive only, a street railway company should not be compelled to continue operation where it can be done only at a loss.⁸⁴ The fact that a city has granted a street car company the right to use streets does not preclude the state from permitting it to take up part of its tracks as un-

⁷⁷ *State v. Gopher Tire & Rubber Co.*, — Minn. —, 177 N. W. 937.

⁷⁸ *State v. Gopher Tire & Rubber Co.*, — Minn. —, 177 N. W. 937.

⁷⁹ *Nebraska State Ry. Commission v. Alfalfa Butter Co.*, — Neb. —, 178 N. W. 766.

⁸⁰ *State ex rel. Rossen v. Welch*, — N. D. —, 172 N. W. 234.

⁸¹ Article on right of public utility to cease operation and dis-

mantle its plant without consent of the state, see 32 *Harvard L. Rev.* 716-720.

⁸² *Lyon & Hoag v. Railroad Commission*, — Cal. —, 190 Pac. 795.

⁸³ *Southwest Missouri R. Co. v. Public Service Commission*, — Mo. —, 219 S. W. 380.

⁸⁴ *Potter Matlock Trust Co. v. Warren County*, 182 Ky. 840, 207 S. W. 709.

profitable.⁸⁵ The public service commission may permit an interurban railway to discontinue unprofitable spur tracks connecting with railroad depots.⁸⁶ In Ohio, by statute, the Public Utilities Commission may authorize abandonment of a part of an interurban line.⁸⁷ The purchaser of a street railroad at a receiver's sale assumes the duty to operate it;⁸⁸ but where a street railway cannot be operated at a profit, the court, in directing a sale by a receiver under foreclosure, may authorize the purchaser either to operate the system or dismantle and remove the physical property, where the charter of the company did not itself require continued operation of the road.⁸⁹ Where an interurban road is in the hands of a receiver, he may, in a proper case, be permitted to cease operation of the road, but not until after such a lapse of time as will enable patrons to adjust themselves to changed conditions; and if one unit of the road was formerly a successful operating unit, discontinuance thereof should not be allowed if it can be run independently.⁹⁰ On forfeiture of a street franchise, a street railway company may tear up its tracks and remove the railway, without restoring the surface of the street to its original condition.⁹¹

A city may compel a gas company to comply with its franchise by restraining it from discontinuing service.⁹²

§ 4425. Regulations imposing penalties—In general. Penalty provisions do not apply, according to the later cases, while suit is pending, in good faith, for the determination of the question of whether the statute is confiscatory.⁹³ Penalties for charging

⁸⁵ Southwest Missouri R. Co. v. Public Service Commission, — Mo. —, 219 S. W. 380.

⁸⁶ Southwest Missouri R. Co. v. Public Service Commission, — Mo. —, 219 S. W. 380.

⁸⁷ Northfield v. Public Utilities Commission, 100 Ohio St. 424, 126 N. E. 311.

⁸⁸ Gress v. Ft. Loramie, 100 Ohio St. 35, 125 N. E. 112.

⁸⁹ Gilchrist v. Waycross St. & S. Ry. Co., 246 Fed. 952.

The purchaser of a street railway should be permitted to discontinue operations where the

road cannot be made to pay. Gress v. Ft. Loramie, 100 Ohio St. 35, 125 N. E. 112.

⁹⁰ New York Trust Co. v. Buffalo & Lake Erie Traction Co., 112 N. Y. Misc. 414, 183 N. Y. Supp. 278.

⁹¹ Mt. Vernon v. Berman & Reed, 100 Ohio St. 1, 125 N. E. 116.

⁹² City of Jamestown v. Pennsylvania Gas Co., 263 Fed. 437.

⁹³ Coal & Coke Ry. Co. v. Conley, 67 W. Va. 129, 67 S. E. 613. See also Bronx Gas & Electric Co. v. Public Service Commission,

rates higher than those fixed by law may be awarded in favor of aggrieved passengers instead of the state, without being contrary to due process of law.⁹⁴

• • § 4427. — **Unreasonable penalties.** Excessive penalties for noncompliance with rate regulations are unconstitutional.⁹⁵ A penalty of not less than fifty nor more than three hundred dollars for charging more than the rate fixed by law, as applied to railroad companies, is not unreasonable.⁹⁶ It cannot be contended that penalties are so severe as to prevent resort to the courts where the penalty provision could have been suspended by injunction in a suit against the state railroad commission.⁹⁷

§ 4428. **Regulations as to employees.** It is within the police power to require public service corporations to give a letter to employees discharged or leaving the service, stating the cause for leaving, etc.⁹⁸ Requiring prompt payment of wages is within the police power.⁹⁹ Requiring all private corporations to pay wages weekly is unconstitutional where there is excepted steam surface railways and corporations engaged in the production of farm and dairy products.¹

§ 4429. — **Amount of wages.**²

§ 4433. **License fees—Where right to use streets has been granted by federal government or by state.**³ A reasonable city tax upon the maintenance of poles and wires of a telegraph company within city limits is not an unwarranted burden on inter-

190 N. Y. App. Div. 13, 180 N. Y. Supp. 38.

⁹⁴ St. Louis, I. M. & S. R. Co. v. Williams, 251 U. S. 63, 63 L. Ed. 139, aff'g 131 Ark. 442, 199 S. W. 376.

⁹⁵ Florida East Coast Ry. Co. v. State, — Fla. —, 83 So. 708.

⁹⁶ St. Louis, I. M. & S. R. Co. v. Williams, 251 U. S. 63, 63 L. Ed. 139, aff'g 131 Ark. 442, 199 S. W. 376.

⁹⁷ St. Louis, I. M. & S. R. Co. v. Williams, 251 U. S. 63, 63 L. Ed.

139, aff'g 131 Ark. 442, 199 S. W. 376.

⁹⁸ Dickinson v. Perry, 75 Okla. 25, 181 Pac. 504.

⁹⁹ Manford v. Menil Singh, 40 Cal. App. 700, 181 Pac. 844.

¹ Anderson v. Uncle Sam Oil Co., 106 Kan. 483, 186 Pac. 198.

² Minimum wage laws as constitutional, see Halcombe v. Creamer, 231 Mass. 99, 120 N. E. 354.

³ See also § 4435, *infra*.

state commerce nor does it infringe rights conferred by act of congress.⁴

§ 4434. — Reasonableness of amount of license.⁵ A license tax on telegraph poles, where reasonable in amount, is not necessarily objectionable because it exceeds the net returns from local business and must be paid from interstate earnings.⁶ An annual occupation tax of \$5 imposed by a town on a telegraph company, on intrastate business, is not shown to be unreasonable by the fact that the gross annual income of the company in the town is only \$70.68.⁷ A license tax of fifty cents a pole is not unreasonable, as applied to a telegraph company, although applicable to poles standing on private property as well as to poles on the streets.⁸ A license fee of one thousand dollars on foreign corporations with a capital over one and not exceeding ten million is not unreasonable.⁹

§ 4435. — Application of rules to particular corporations. A city may impose a reasonable license tax on each pole of a telegraph company, although engaged in interstate commerce, both as rental and to cover expense of inspection, etc.¹⁰ The fact that a city license tax is imposed upon poles of a telegraph company that stand on a railroad right of way as well as those that stand on the streets does not invalidate the tax, since imposed in part for the special cost of supervising and regulating the poles.¹¹

§ 4436. Regulations of railroad companies—In general. Contract rights of a railroad company as to operation of a track in

⁴ Mackay Telegraph & Cable Co. v. Little Rock, 250 U. S. 94, 63 L. Ed. 863, aff'g 131 Ark. 306, 199 S. W. 90.

⁵ Fee of two dollars for each telegraph pole held not unreasonable in Postal Telegraph-Cable Co. v. Richmond, 249 U. S. 252, 63 L. Ed. 590.

⁶ Postal Telegraph-Cable Co. v. Richmond, 249 U. S. 252, 63 L. Ed. 590.

⁷ Dexter v. Western U. Tel. Co., — Ga. —, 103 S. E. 430.

⁸ Mackay Telegraph & Cable Co.

v. Little Rock, 250 U. S. 94, 63 L. Ed. 863, aff'g 131 Ark. 306, 199 S. W. 90.

⁹ General Railway Signal Co. v. Virginia, 246 U. S. 500, 62 L. Ed. 854, aff'g 118 Va. 301, 87 S. E. 598, and see §§ 4605, 4651, *infra*.

¹⁰ Postal Telegraph-Cable Co. v. City of Richmond, 249 U. S. 252, 63 L. Ed. 590.

¹¹ Mackay Telegraph & Cable Co. v. Little Rock, 250 U. S. 94, 63 L. Ed. 863, aff'g 131 Ark. 306, 199 S. W. 90.

a public street are subject to the police power to secure public safety.¹² A statute requiring separate coaches for white and black persons is valid.¹³ A penalty may be imposed on railways running trains of more than seventy cars.¹⁴

It is not an unreasonable exercise of the police power to require removal of a track used by a railroad company only to serve abutting private industries, at a street crossing near the Denver Union Depot, for the safety of the public where the resulting expense and loss of revenue would be small.¹⁵

A railroad company cannot be compelled to instal cattle scales at a station, for the purpose of building up the cattle trading business at that point, although the public may be greatly benefited thereby.¹⁶

A railroad company, in addition to being required to erect depots at stations, may be compelled to furnish an agent at such depots.¹⁷ The volume of outgoing freight at a station is not necessarily the criterion to determine the reasonableness of an order requiring the maintenance of an agent at such station.¹⁸

§ 4437. — Requiring extension of line. A railroad company may be required to extend a sidetrack leading to a manufacturing plant, so as to meet the necessities of an enlargement of the plant, and to bear a reasonable part of the cost of extension.¹⁹

¹² *Denver & R. G. R. Co. v. Denver*, 250 U. S. 241, 63 L. Ed. 958, aff'g 63 Colo. 574, 167 Pac. 969.

¹³ *South Covington & C. St. R. Co. v. Com.*, 181 Ky. 449, 205 S. W. 603.

¹⁴ See *Arizona Eastern R. Co. v. State*, 19 Ariz. 409, 171 Pac. 906.

¹⁵ *Denver & R. G. R. Co. v. Denver*, 250 U. S. 241, 63 L. Ed. 958, aff'g 63 Colo. 574, 167 Pac. 969.

¹⁶ *Great Northern R. Co. v. Cahill*, 253 U. S. 71, 64 L. Ed. 787, rev'g 40 S. D. 55, 166 N. W. 306, and explaining *Great Northern R. Co. v. Minnesota*, 238 U. S. 340, 59 L. Ed. 1337.

¹⁷ *Aandahl v. Great Northern Ry. Co.*, — N. D. —, 171 N. W.

628; *Angelina & N. R. R. Co. v. Railroad Commission*, — Tex. Civ. App. —, 212 S. W. 703.

¹⁸ *Louisiana Ry. & Nav. Co. v. Railroad Commission*, 146 La. 609, 83 So. 849.

¹⁹ *Chicago & N. W. Ry. Co. v. Ochs*, 249 U. S. 416, 63 L. Ed. 679, aff'g 135 Minn. 323, Ann. Cas. 1918 E 337, 160 N. W. 866. To same effect, see *Lake Erie & W. R. Co. v. Public Utilities Commission*, 249 U. S. 422, 63 L. Ed. 684, aff'g 277 Ill. 574, 115 N. E. 519.

Requiring rapid transit company to build extensions, see *Allied-Associations of West Philadelphia v. Public Service Commission*, 70 Pa. Super. Ct. 13.

“Power of public service com-

§ 4438. — **Requiring operation of road or of trains.**²⁰ An order requiring separate trains for freight and passengers is unreasonable where the road does not pay expenses.²¹

It has been held that a common carrier cannot be compelled by a state to continue operation of its railroad at a loss,²² but it has also been held that inability to operate a railway at the then rate of fare without loss does not excuse failure to discharge the duty owing the public.²³ A railroad company cannot discontinue operations and dismantle the road without the consent of the state;²⁴ but consent of the public service commission is not necessary to authorize a railway company to discontinue business, after dissolution of the corporation by a court.²⁵ A public service commission may prevent the removal or abandonment of a railroad which is in use.²⁶ A railroad company, even where in the hands of a receiver, may be compelled to operate the road, in a proper case.²⁷ A company operating a railroad through a lessee company cannot prevent obedience to an order requiring it to operate the road by claiming it was not author-

mission to require railroad or street railway to extend its line or build new line to new territory," see note in 2 A. L. R. 983.

²⁰ Reasonableness of order requiring re-establishment of two passenger trains, see *State ex rel. Railroad Com'rs v. South Georgia Ry. Co.*, — Fla. —, 85 So. 663.

²¹ *Marshall v. Bush*, 102 Neb. 279, L. R. A. 1918 E 385, 167 N. W. 59.

²² *Brooks-Scanlon Co. v. Railroad Commission*, 251 U. S. 396, 64 L. Ed. 323, rev'g 144 La. 1086, 81 So. 727.

²³ *Public Service Commission v. International Ry. Co.*, 185 N. Y. App. Div. 220, 172 N. Y. Supp. 551.

²⁴ *Gasser v. Garden Bay R. Co.*, 205 Mich. 5, 171 N. W. 791.

A railroad cannot abandon industrial spur tracks, in Missouri, without leave of the public service commission which need not neces-

sarily consent thereto because operation of such spur tracks is unprofitable. *State ex rel. Public Service Commission v. Missouri Southern R. Co.*, 279 Mo. 455, 214 S. W. 381.

²⁵ *New York & P. Ry. Co. v. Public Service Commission*, 72 Pa. Super. Ct. 523.

²⁶ *Brooks-Scanlon Co. v. Railroad Commission*, 144 La. 1086, 81 So. 727, where logging and saw-mill company was held properly required to continue operation of a railroad.

The public service commission, and not the courts, has the power, in Colorado, to permit a railroad company to abandon its road and dismantle it. *People v. Colorado Title & Trust Co.*, 65 Colo. 472, 178 Pac. 6.

²⁷ *Central Bank & Trust Co. v. Greenville & W. R. Co.*, 248 Fed. 350.

ized to engage in the railroad business.²⁸ Foreclosure purchasers of a railroad will not be required to rehabilitate the road at a large cost, and operate it, where past experience shows it cannot be operated at a profit.²⁹ Where the state is not a party to the proceeding, a court of equity, in enforcing contract liens upon railroad property, has no power to order the operation of the road discontinued and its sale as junk.³⁰

§ 4439. — Requiring stopping of trains at stations.³¹ Interstate trains cannot be compelled to stop where reasonable local service is provided.³² But an interstate passenger train may be compelled to make local stops on flag, where reasonable, and the point is not otherwise furnished adequate service.³³ Where reasonable, interstate trains may be compelled to stop at a county seat of only 1500 population.³⁴ An order requiring a railroad to reroute two local passenger trains daily away from a cut-off, as incidental to requiring them to stop at a city, where reasonable, is a proper regulation.³⁵

§ 4440. — Regulations as to depots. The reasonableness of an order requiring a railroad company to construct a depot at a particular place depends on the facts of the particular case.³⁶ Wharf and depot facilities should be ordered of a railroad

²⁸ *Brooks-Scanlon Co. v. Railroad Commission*, 144 La. 1086, 81 So. 727.

²⁹ *State ex rel. Brown v. Beaton*, — Iowa —, 178 N. W. 1.

³⁰ *Anderson v. Dent*, — Fla. —, 85 So. 151.

³¹ Reasonableness of requiring stopping of two trains daily, on flag, see *Kansas City Southern Ry. Co. v. State*, — Okla. —, 178 Pac. 662.

³² *Chicago, R. I. & P. Ry. Co. v. State*, — Okla. —, 175 Pac. 199.

³³ *State ex rel. Missouri, K. & T. R. Co. v. Public Service Commission*, 277 Mo. 175, 210 S. W. 386.

³⁴ *Gulf, C. & S. F. R. Co. v. State*

of Texas, 246 U. S. 58, 62 L. Ed. 575, aff'g — *Tex. Civ. App.* —, 169 S. W. 385.

³⁵ *Lusk v. Public Service Commission*, 277 Mo. 264, 210 S. W. 72.

³⁶ *Railroad Commission v. Pecos & N. T. Ry. Co.*, — *Tex. Civ. App.* —, 212 S. W. 535.

Requiring new depot, see *Commercial Club v. Chicago, St. P., M. & O. R. Co.*, 142 Minn. 169, 171 N. W. 312.

Requiring moving of depot and erection of new one as unreasonable, see *Atchison, T. & S. F. R. Co. v. Wolverton*, — Okla. —, 171 Pac. 722.

company only so far as reasonable, taking into consideration the expense, probable growth of business, etc.³⁷

§ 4441. — Regulating running time of trains. A state cannot fix the time allowed for stops of trains in the course of interstate transit, where unreasonable.³⁸

§ 4442. — Requiring connections with other roads. Railroad companies may be compelled to construct a connecting track.³⁹

§ 4443. — Requiring construction of spur tracks. The state may compel a railroad company to build spur tracks, where reasonable.⁴⁰

§ 4444. — Regulations as to grade crossings. The state may require railroads to build bridges to carry the street across railroad tracks,⁴¹ or to construct a sidewalk across its tracks at a village street crossing,⁴² or to separate grade crossings.⁴³ It cannot be compelled to elevate its tracks in a certain district, where unreasonable.⁴⁴ A railroad company has no vested right to insist that a rule of law applicable to the assessment of damages in a proceeding to appropriate a crossing to which a junior company was entitled, should not be changed by statute or by court decision.⁴⁵

³⁷ State ex rel. Railroad Com'rs v. Atlantic Coast Line R. Co., 77 Fla. 366, 81 So. 498.

³⁸ Missouri, K. & T. Ry. Co. v. State of Texas, 245 U. S. 484, 62 L. Ed. 419, L. R. A. 1918 C 535, rev'g — Tex. Civ. App. —, 167 S. W. 822.

³⁹ Commercial Club City of Mitchell v. Chicago, M. & St. P. R. Co., 41 S. D. 314, 170 N. W. 149. See also Chicago, I. & L. R. Co. v. Public Service Commission, 188 Ind. 334, 121 N. E. 276.

⁴⁰ Railroad Commission v. Louisville & N. R. Co., 148 Ga. 442, 96 S. E. 855.

Order requiring new station and industrial sidetrack as reasonable,

see Chicago, B. & Q. R. Co. v. Public Utilities Commission, — Colo. —, 190 Pac. 539.

⁴¹ Powell v. Seaboard Air Line R. Co., 178 N. C. 243, 100 S. E. 424; Chicago, R. I. & P. R. Co. v. Taylor, — Okla. —, 192 Pac. 349.

⁴² Great Northern R. Co. v. Minnesota ex rel. Village of Clara City, 246 U. S. 434, 62 L. Ed. 817, aff'g 132 Minn. 474, 157 N. W. 1069; s. c., 130 Minn. 480, L. R. A. 1918 D 1153, 153 N. W. 879.

⁴³ Chicago, M. & St. P. R. Co. v. Lake County, 287 Ill. 337, 122 N. E. 526.

⁴⁴ Hines v. Clarendon Levee Dist., 264 Fed. 127.

⁴⁵ Northern Pac. R. Co. v. Puget

§ 4445. — Requiring lighting of tracks. While a state or municipality may require a railroad company to pay the entire cost of lighting a street under a viaduct, where the viaduct makes more light necessary, it cannot require it to light adjacent streets if the presence of the road does not require more light than would otherwise be necessary.⁴⁶

§ 4446. — Regulating rate of speed. It is proper to regulate the rate of speed of railroads, in municipalities, at crossings, etc.⁴⁷ A six-mile speed ordinance in a town of 2,600 is not unreasonable.⁴⁸

§ 4448. — Requiring signals or flagmen. The legislature may prescribe the manner in which railroads shall give warnings at crossings.⁴⁹

§ 4450. — Requiring fencing of tracks and building of cattle guards. Railroad companies may be required to construct wing fences and cattle guards.⁵⁰ Requiring payment of attorney fees by railroad company where injury results from failure to fence is a proper exercise of the police power.⁵¹

§ 4451. — Regulations as to sleeping car service.⁵²

§ 4452. Regulations of street railroad companies. A city may require all traffic, including street cars, on entering a public square, to turn to the right and pass around the square.⁵³ Re-

Sound & W. H. R. Co., 250 U. S. 332, 63 L. Ed. 1013, aff'g State ex rel. Puget Sound & W. H. R. Co. v. Northern Pac. R. Co., 94 Wash. 10, 161 Pac. 850, 97 Wash. 701, 166 Pac. 793.

⁴⁶ Washington Terminal Co. v. District of Columbia, 265 Fed. 965, criticizing Chicago v. Pennsylvania Co., 252 Ill. 185, 36 L. R. A. (N.S.) 1081, Ann. Cas. 1912 D 400, 96 N. E. 833.

⁴⁷ Shortino v. Salt Lake & U. R. Co., 52 Utah 476, 174 Pac. 860.

⁴⁸ Murrell v. Kansas City Southern R. Co., 279 Mo. 173, 213 S. W. 964.

⁴⁹ Hurt v. Yazoo & M. V. R. Co., 140 Tenn. 623, 205 S. W. 437; Gordon v. Illinois Cent. R. Co., 168 Wis. 244, 169 N. W. 570.

⁵⁰ Dwyer v. Chicago & N. W. Ry. Co., 41 S. D. 535, 171 N. W. 760.

⁵¹ Hindman v. Oregon Short Line R. Co., 32 Idaho 133, 178 Pac. 837.

⁵² Order requiring additional Pullman service as unreasonable, see Atchison, T. & S. F. R. Co. v. State, — Okla. —, 176 Pac. 393.

⁵³ Easton v. Miller, 265 Pa. 25, 108 Atl. 262.

quiring street cars to stop at every intersection, on signal, is reasonable.⁵⁴ A street railway company may be compelled to relocate its tracks, if not unreasonable.⁵⁵ Municipal regulations requiring exercise of the greatest care when one street car approaches another which has stopped are reasonable.⁵⁶ Requiring each street car to be operated by a motorman and conductor is not unreasonable, where substitute devices for operation by one man are not clearly shown to be as safe and convenient for passengers.⁵⁷

A regulation of the speed of street cars is *prima facie* reasonable.⁵⁸ Limiting speed of street cars to fifteen miles an hour is not unreasonable.⁵⁹

An ordinance requiring street railroads to sprinkle their tracks is not unreasonable nor discriminating because not applied to other vehicles using the streets.⁶⁰

Police power may be exercised by requiring street railways to pave between the tracks and a foot outside.⁶¹ A city requirement that the railroad zone be paved like the rest of the street with asphalt upon a concrete foundation, was not unreasonable, the duty to pave being fixed by the franchise.⁶² A mortgage on street railway property is subject to franchise conditions such as the duty to pave streets.⁶³ Where a city has collected the cost of paving from benefited property, it cannot compel a street railway to pay for the cost of the paving between its tracks.⁶⁴ A city, after having removed a street pavement to make a sewer improvement, may, under the New York statutes,

⁵⁴ *People v. Detroit United Ry.*, 207 Mich. 143, 173 N. W. 396.

⁵⁵ *Connecticut Co. v. Stamford*, — Conn. —, 110 Atl. 554.

⁵⁶ *Leis v. Cleveland Ry. Co.*, — Ohio St. —, 128 N. E. 73.

⁵⁷ *Sullivan v. Shreveport*, 251 U. S. 169, 63 L. Ed. 205, aff'g 142 La. 573, 77 So. 286.

⁵⁸ *Puget Sound Elec. Ry. v. Benson*, 253 Fed. 710.

⁵⁹ *Mobile Light & Railroad Co. v. R. O. Harris Grocery Co.*, — Ala. App. —, 84 So. 867.

⁶⁰ *Pacific Gas & Electric Co. v. Police Court City of Sacramento*,

251 U. S. 22, 64 L. Ed. 112, aff'g 28 Cal. App. 412, 152 Pac. 928.

⁶¹ *Wheeling Traction Co. v. Board of Com'rs*, 248 Fed. 205.

Paving, duty as to under certain ordinances, see *Burlington Railway & Light Co. v. Burlington*, — Iowa —, 176 N. W. 285.

⁶² *Milwaukee Elec. Railway & Light Co. v. Wisconsin ex rel. City of Milwaukee*, 252 U. S. 100, 64 L. Ed. 476, aff'g 166 Wis. 163, 164 N. W. 844.

⁶³ *Faller v. Boisot*, 249 Fed. 193.

⁶⁴ *Duluth v. Duluth St. R. Co.*, — Minn. —, 176 N. W. 47.

require a street railway company to restore the pavement between its tracks and two feet on each side.⁶⁵

Where a New York subway franchise gave the right to use city sidewalks for exits and entrances to the subway, the city could not compel relocation of exits at the subway's expense, and the city could change entrances and exits only at its own expense.⁶⁶

In Washington, the public service commission cannot relieve a street car company from franchise provisions as to paving, paying a certain per cent of gross earnings to the city, etc., although the income is not sufficient to pay a reasonable return on the value of the property.⁶⁷ The fact that a corporate business fails to earn six per cent upon the value of the property used does not permit the company to escape a contractual duty to pave a part of the street.⁶⁸

The "Power of public service commission with respect to regulation of street railways," including rates, is the subject of a recent extended note in the American Law Reports.⁶⁹

§ 4453. Regulations of telegraph, telephone and electric light companies—In general. A state cannot impose penalties for failure of telegraph companies to make prompt delivery of interstate messages, since such companies are regulated by federal statutes.⁷⁰ In New York, the public service commission cannot require a telegraph company to extend credit to another telegraph company for which it transmits messages, although it extends credit to others, since relating to a matter with which the public is not concerned.⁷¹ Fixtures of a lighting company

⁶⁵ New York v. Whitridge, 227 N. Y. 180, 124 N. E. 788.

⁶⁶ New York City v. Hudson & M. R. Co., 188 N. Y. App. Div. 294, 177 N. Y. Supp. 4.

⁶⁷ State ex rel. Tacoma Railway & Light Co. v. Public Service Commission, 101 Wash. 601, 172 Pac. 890.

⁶⁸ Milwaukee Elec. Ry. & Light Co. v. Wisconsin ex rel. City of Milwaukee, 252 U. S. 100, 64 L. Ed. 476, aff'g 166 Wis. 163, 164 N. W. 844.

⁶⁹ 5 A. L. R. 36, annotating Puget Sound Traction, Light & Power Co. v. Public Service Commission, 100 Wash. 329, 5 A. L. R. 30, 170 Pac. 1014.

⁷⁰ Western U. Tel. Co. v. Boegli, 251 U. S. 315, 64 L. Ed. 281.

⁷¹ People ex rel. Western U. Tel. Co. v. Public Service Commission, 192 N. Y. App. Div. 748, 183 N. Y. Supp. 659.

using streets under a franchise cannot be displaced or removed merely to establish a city lighting system.⁷²

§ 4454. — Regulations as to poles and wires. In the exercise of its police power, a state may change a statute providing that the mode of using village streets by electric light and power companies shall be determined by the probate court in case of disagreement, by leaving sole control in the city and forbidding erection of poles and wires without its consent, as against the objection of existing franchise holders.⁷³

§ 4455. — Requiring wires to be put underground. A city may require a telegraph company to put its wires underground.⁷⁴

§ 4456. — Requiring physical connection of lines. Telephone companies may be required to establish connections,⁷⁵ but not where they work a discrimination against the subscribers of either company.⁷⁶ In requiring physical connection of telephone wires, the order cannot compel business intercourse between two competing companies to the detriment of either.⁷⁷ For instance, a state cannot compel physical connection between competing telephone lines where one has long distance as well as local lines and the order would permit the one having only local lines to have the benefit of the other's lines to its detriment without compensation.⁷⁸

⁷² *Los Angeles v. Los Angeles Gas & Electric Co.*, 251 U. S. 32, 63 L. Ed. 121, aff'g 241 Fed. 912.

⁷³ *Hardin-Wyandot Lighting Co. v. Upper Sandusky*, 251 U. S. 173, 63 L. Ed. 210, aff'g 93 Ohio St. 428, 113 N. E. 402.

⁷⁴ *Oil City v. Postal Telegraph Cable Co.*, 68 Pa. Super. Ct. 77.

⁷⁵ *Northern Indiana & Southern Michigan Telephone, Telegraph & Cable Co. v. People's Mut. Tel. Co.*, 187 Ind. 486, 119 N. E. 212; *Pioneer Telephone & Telegraph Co. v. State*, 78 Okla. 38, 188 Pac. 107; *Southwestern Telephone & Telegraph Co. v. State*, 109 Tex. 337, 207 S. W. 308.

Physical connections between telephone lines, exclusive jurisdiction of railroad commission, see *Oceana Farmers' Mut. Tel. Co. v. United Home Tel. Co.*, 205 Mich. 662, 172 N. W. 553.

⁷⁶ *Pioneer Telephone & Telegraph Co. v. State*, — Okla. —, 177 Pac. 580.

⁷⁷ *Pioneer Telephone & Telegraph Co. v. State*, 77 Okla. 216, 186 Pac. 934.

⁷⁸ *Pioneer Telephone & Telegraph Co. v. State*, 77 Okla. 216, 186 Pac. 934.

§ 4457. Regulation of gas companies. The public service commission may, at least in some states, require a gas company to refund a certain per cent of monthly bills for failure to furnish adequate service.⁷⁹

§ 4461. Regulation of mining companies. Requiring wash rooms for mine, etc., employees is a valid police regulation.⁸⁰

VII. REGULATION OF RATES

A. Right to Regulate and General Considerations

§ 4468. Power to require and regulate street car transfers. A transfer system between two street railroads may be ordered.⁸¹

§ 4469. Power as extending to increasing as well as reducing rates. Power of the state to regulate rates includes power to increase as well as to reduce them,⁸² and a public service commission may increase as well as lower rates.⁸³ Where a city council increased the rate of fare on a street railroad, but expressly subject to revocation at any time, the street car company cannot object to such a revocation.⁸⁴

§ 4470. Particular companies whose rates may be regulated. Fire insurance rates may be regulated,⁸⁵ as may the charges of public stock yard companies.⁸⁶

§ 4471. Rates of municipal plants. In some jurisdictions, rates of municipally owned public utilities may be regulated by the state,⁸⁷ while in other jurisdictions rates of a municipal

⁷⁹ Oklahoma Natural Gas Co. v. State, 78 Okla. 5, 188 Pac. 338.

⁸⁰ People v. Cleveland, C., C. & St. L. R. Co., 288 Ill. 523, 123 N. E. 579.

⁸¹ Tulsa St. R. Co. v. Union Ry. Co., 76 Okla. 102, 184 Pac. 71.

⁸² International R. Co. v. Public Service Commission, 226 N. Y. 474, 124 N. E. 123.

⁸³ In re Petition for Increase of Street Car Fares, 179 N. C. 151, 101 S. E. 619.

⁸⁴ Michigan Ry. Co. v. Lansing, 260 Fed. 322.

⁸⁵ State ex rel. Waterworth v. Harty, 278 Mo. 685, 213 S. W. 443.

⁸⁶ Union Stockyards Co. v. Nebraska State Ry. Commission, 103 Neb. 224, 170 N. W. 908, 172 N. W. 528.

⁸⁷ Springfield Gas & Electric Co. v. Springfield, 292 Ill. 236, 126 N. E. 739.

plant are not subject to regulation by the state.⁸⁸ A statute giving the public service commission control over electric corporations does not give the right to regulate an electric plant owned by a city.⁸⁹

§ 4473. Fixing rates by contract as distinguished from "regulation" of rates independently of agreement—Power of municipality to "contract" as to rates.⁹⁰ Even though a municipality has no delegated power to contract as to rates on granting a franchise, so as to bind the state, it seems that it may so contract as to bind the parties in the absence of governmental interposition.⁹¹ In Iowa, municipalities cannot contract as to public utility rates, and hence franchise rates are not binding on either the municipality or the public utility company.⁹²

§ 4474. — Company as precluded from denying power to contract or reasonableness of rates. Rates agreed on by contract cannot be claimed to be confiscatory,⁹³ and franchise rates cannot be disregarded by the public service company.⁹⁴ A franchise contract fixing rates, made when the city had no power to make it, cannot be questioned by the city where it treated it as valid for many years after the enactment of a statute giving it the power to make such a contract.⁹⁵ A public service company cannot,

⁸⁸ Barnes Laundry Co. v. City of Pittsburgh, 266 Pa. 24, 109 Atl. 535.

⁸⁹ City of Pasadena v. Railroad Commission, — Cal. —, 192 Pac. 25.

⁹⁰ See also § 4490, *infra*.

Contract between town and water company held not to fix rates for twenty years, in Oak Bluffs v. Cottage City Water Co., — Mass. —, 126 N. E. 384.

A company operating under two city franchises, one of which was acquired by assignment, can charge only the lowest rates provided in either franchise. Southwestern Gas & Electric Co. v. City of Shreveport, 261 Fed. 771.

Construction of bridge charter of corporation, of 1795, as to tolls

for automobiles, see Proprietors of Cornish Bridge v. Fitts, — N. H. —, 107 Atl. 626.

⁹¹ Milwaukee Elec. Railway & Light Co. v. Railroad Commission of Wisconsin, 238 U. S. 174, 59 L. Ed. 1254; Traverse City v. Michigan Railroad Commission, 202 Mich. 575, 168 N. W. 481.

⁹² Woodward v. Iowa Railway & Light Co., — Iowa —, 178 N. W. 549.

⁹³ Borough of Belle Plaine v. Northern Power Co., 142 Minn. 361, 172 N. W. 217, quoting 4 McQuillin Mun. Corp., § 1741.

⁹⁴ Bismarck Gas Co. v. District Court, —N. D. —, 170 N. W. 878.

⁹⁵ Omaha Gas Co. v. Omaha, 249 Fed. 350.

while claiming benefits under a street franchise fixing a maximum rate of fare, attack such rate on the ground that the municipality had no power to contract as to rates.⁹⁶ A contract between a city and a gas company fixing rates is not unenforceable because unreasonable; and even if it was, the unreasonableness must be determined as of the time the contract was made and not thereafter.⁹⁷

§ 4475. Penalties for violation of rate laws.⁹⁸

B. Who May Regulate Rates

§ 4477. **United States.** Congress, in the exercise of its war power, had the right to suspend state maximum rate statutes.⁹⁹ Also, in terminating federal control of railroads, it had power to provide that state maximum rate statutes would not be automatically revived.¹

§ 4478. **State.**² Rates of telephone and telegraph companies were not subject to regulation by the state during the world war.³ A state cannot regulate telephone rates for intrastate business over lines taken over into the possession of the United States as a war measure, and which by the exercise of its governmental authority it operates and controls.⁴

§ 4479. **Public service commission.**⁵ The legislature has power to fix the rates as to some companies and provide a subordinate

⁹⁶ *Meridian Light & Railway Co. v. City of Meridian*, 265 Fed. 765.

⁹⁷ *Lenawee County Gas & Electric Co. v. Adrian*, 209 Mich. 52, 176 N. W. 590.

⁹⁸ See §§ 4425-4427, *supra*.

⁹⁹ *Public Service Commission v. New York Cent. R. Co.*, 112 N. Y. Misc. 617, 183 N. Y. Supp. 799.

¹ *Public Service Commission v. New York Cent. R. Co.*, 112 N. Y. Misc. 617, 183 N. Y. Supp. 799.

² For article on new limitations upon state regulation of railroad rates, see 20 *Columbia L. Rev.* 660-679.

³ "Exercise of rate-making power

as illegal interference with corporate management of a public utility," see note in *L. R. A.* 1918 F 277, annotating *State ex rel. Railroad Com'rs v. Florida East Coast R. Co.*, 69 Fla. 480, *L. R. A.* 1918 F 272, 68 So. 729.

³ *State ex rel. Cities of Seattle & Tacoma v. Public Service Commission*, — Wash. —, 188 Pac. 7.

⁴ *Dakota Central Tel. Co. v. South Dakota ex rel. Payne*, 250 U. S. 163, 63 L. Ed. 910, rev'g 41 S. D. 460, 171 N. W. 277. *Contra*, *State ex rel. Collins v. Cumberland Telephone & Telegraph Co.*, 120 Miss. 325, 81 So. 404, 82 So. 311.

⁵ Powers of public service com-

body to fix the rate as to others.⁶ Franchise contracts as to rates cannot be abrogated by a public service commission where such power has not been delegated to it.⁷ If the legislature has fixed a maximum rate, the public service commission cannot increase it.⁸ In New York, a gas company cannot increase franchise rates without an order of the public service commission.⁹ In Washington, because of a statute limiting street car fares to five cents, the public service commission cannot raise the fare above five cents.¹⁰ In West Virginia, the public service commission may regulate gas rates charged to manufacturing consumers as well as those charged to others.¹¹

§ 4480. Municipal corporation—In general. A municipality cannot “regulate” rates of public service corporations unless

missions as to rates in general, see *In re Searsport Water Co.*, 118 Me. 382, 108 Atl. 452; *In re Guilford Water Co.’s Service Rates*, 118 Me. 367, 108 Atl. 446.

Power to fix rates as between city and public service commission, see *Pueblo v. Public Utilities Commission*, — Colo. —, 187 Pac. 1026; *Cleveland Tel. Co. v. Cleveland*, 98 Ohio St. 358, 121 N. E. 701.

As to effect of agreement between public service commission and public service corporation as to change of rates fixed by contract with city, where city objects to change, see *City of Salem v. Salem Water, Light & Power Co.*, 255 Fed. 295.

For note on “Jurisdiction of Public Utilities Commission over rates as limited by constitutional or statutory power of municipality to regulate utilities,” see *L. R. A.* 1918 D 315.

⁶ *Bronx Gas & Electric Co. v. Public Service Commission*, 190 N. Y. App. Div. 13, 180 N. Y. Supp. 38.

⁷ *Niagara Falls v. Public Serv-*

ice Commission, — N. Y. —, 128 N. E. 247, aff’g 190 N. Y. App. Div. 890, 178 N. Y. Supp. 882.

⁸ *Public Service Commission v. Kings County Lighting Co.*, 105 N. Y. Misc. 665, 173 N. Y. Supp. 789.

⁹ *North Hempstead v. Public Service Co.*, 193 N. Y. App. Div. 224, 183 N. Y. Supp. 788; *Village of Mt. Morris v. Pavilion Nat. Gas Co.*, 183 N. Y. Supp. 792.

Power as to gas rates as between legislature and public service commission, see *People ex rel. Municipal Gas Co. of Albany v. Public Service Commission*, 224 N. Y. 156, 120 N. E. 132.

Power of commission to fix gas rates in New York, see *Bronx Gas & Electric Co. v. Public Service Commission*, 108 N. Y. Misc. 180, 178 N. Y. Supp. 172.

¹⁰ *State ex rel. Tacoma Railway & Power Co. v. Public Service Commission*, 101 Wash. 601, 172 Pac. 890.

¹¹ *Clarksburg Light & Heat Co. v. Public Service Commission*, — W. Va. —, 100 S. E. 551.

the power so to do has been delegated to it.¹² In Denver, telephone rates may be regulated by the city but not by the public utilities commission.¹³ Fixing telephone rates is not exclusively the power of the city of Detroit under its home rule charter.¹⁴ Under the Michigan statute prohibiting the amendment of any public utility franchise without submission to the electors of the city, a city council cannot approve even a temporary increase in street railroad fares in excess of the rates fixed in the franchise, without submission to the people.¹⁵

§ 4482. — Particular delegations of power. A city cannot regulate gas rates unless power to do so has been delegated; and mere power to provide for the use, regulation and control of streets is not sufficient.¹⁶ Delegation of power to a city to grant water companies rights of way in the streets, and to supervise and control their use, confers no power to regulate rates.¹⁷

§ 4483. — Regulating rates outside municipality. Of course a city cannot contract as to rates outside the municipality.¹⁸

§ 4484. Courts. The right to fix rates is not in the courts but in the legislature.¹⁹ A court has no authority to fix rates.²⁰ A court cannot authorize its receiver for a street railway to charge a higher rate of fare than the maximum fixed by the franchise.²¹

However, in New York, under the statute relating to gas

¹² Georgia Railway & Power Co. v. Railroad Commission, 149 Ga. 1, 5 A. L. R. 1, 98 S. E. 696.

¹³ Denver v. Mountain States Telephone & Telegraph Co., 67 Colo. 225, 184 Pac. 604.

¹⁴ City of Detroit v. Michigan Railroad Commission, 209 Mich. 395, 177 N. W. 306.

¹⁵ Michigan Ry. Co. v. Lansing, 260 Fed. 322.

¹⁶ City of Kalamazoo v. Titus, 208 Mich. 252, 175 N. W. 480.

¹⁷ City of Winchester v. Winchester Water Works Co., 251 U. S. 192, 63 L. Ed. 221.

¹⁸ Koehn v. Public Service Commission, 107 N. Y. Misc. 151, 176 N. Y. Supp. 147.

¹⁹ State ex rel. Waterworth v. Harty, 278 Mo. 685, 213 S. W. 443; Bronx Gas & Electric Co. v. Public Service Commission, 190 N. Y. App. Div. 13, 180 N. Y. Supp. 38.

²⁰ City of New York v. Bronx Gas & Electric Co., 113 N. Y. Misc. 166, 184 N. Y. Supp. 658.

²¹ Gas & Electric Securities Co. v. Manhattan & Queens Traction Corporation, 253 Fed. 453.

corporations, it has been held that the court may itself fix a fair rate where not so fixed by the legislature and where the public service commission has no jurisdiction to fix the rate.²²

C. Regulation of Rates as Violating Constitutional Provisions

§ 4485. Interference with interstate commerce. The transmission and sale of natural gas produced in one state, and transported by pipe lines and directly furnished to consumers in another state, is interstate commerce; but rates for gas may be fixed by the state where it is consumed, since the rates of gas companies transmitting gas in interstate commerce are not only not regulated by Congress but the Interstate Commerce Act expressly withholds the subject from federal control.²³ The mere intention of a shipper, a circus company, to continue its tour beyond the state, does not convert a contemplated intrastate shipment into one that is interstate, so as to prevent the state regulating the charge.²⁴ A movement of rough lumber from the woods to milling points in the same state, where it remains for some months in the process of manufacture before being sold and shipped as finished products to purchasers and destinations previously unidentified, is not a movement in interstate commerce.²⁵

An order of the Interstate Commerce Commission as to railroad rates, in order to cover intrastate rates fixed by state authority, must have a definite field of operation and not leave uncertain the territory or points to which it applies.²⁶

²² *Morrell v. Brooklyn Borough Gas Co.*, 113 N. Y. Misc. 65, 184 N. Y. Supp. 651.

²³ *Pennsylvania Gas Co. v. Public Service Commission*, 252 U. S. 23, 64 L. Ed. 434, aff'g 225 N. Y. 397, 122 N. E. 260, which aff'd 184 N. Y. App. Div. 556, 171 N. Y. Supp. 1028.

While transportation of gas through pipe lines from one state to another is interstate commerce, yet the sale and delivery of gas to their customers by the local companies operating under special franchises constitutes no part of

such interstate commerce since interstate movement ended when the gas passed into local mains, and hence the state may regulate gas rates. *Public Utilities Commission v. Landon*, 249 U. S. 236, 63 L. Ed. 577.

²⁴ *Southern Pac. Co. v. Arizona*, 249 U. S. 472, 63 L. Ed. 713, aff'g 19 Ariz. 20, 165 Pac. 303.

²⁵ *Arkadelphia Milling Co. v. St. Louis Southwestern R. Co.*, 249 U. S. 134, 63 L. Ed. 517.

²⁶ *Illinois Cent. R. Co. v. Public Utilities Commission of Illinois*, 245 U. S. 493, 62 L. Ed. 425.

§ 4486. Due process of law. Where rates fixed by the state are confiscatory, they may be set aside by the courts.²⁷

§ 4487. Denial of equal protection of the laws.²⁸ A statute fixing railroad rates is not void for unreasonable discrimination because it excepts from the rate thereby fixed, carriers earning over \$8,000 per mile, where it provides that carriers earning more than \$10,000 per mile can charge only two cents per mile instead of two and one-half.²⁹

§ 4488. Impairment of obligation of contract—In general.³⁰ Of course no rate contract can be deemed violated unless there is an existing contract.³¹ The tendency of the courts is to destroy the effect of franchise limitations as to rates fixed by municipalities. While the general rule, often stated and applied, is that a contract of a municipality as to rates cannot be impaired by the city or state by subsequently changing the rates,³² there

²⁷ *Westinghouse Elec. & Mfg. Co. v. Binghamton Ry. Co.*, 255 Fed. 378.

²⁸ See also § 4403 et seq., *supra*.

²⁹ *Attorney General v. Detroit United Ry.*, 210 Mich. 227, 177 N. W. 726, 1023.

³⁰ "Power of public service commission to increase franchise rates," see note under that title in 3 A. L. R. 730.

³¹ *People ex rel. New York, W. & B. Ry. Co. v. Public Service Commission*, — N. Y. App. Div. —, 183 N. Y. Supp. 473.

³² *Greensburg Water Co. v. Lewis*, — Ind. —, 128 N. E. 103; *Ottumwa Railway & Light Co. v. Ottumwa*, — Iowa —, 173 N. W. 270; *People ex rel. City of New York v. Nixon*, 109 N. Y. Misc. 7, 179 N. Y. Supp. 82; *International R. Co. v. Rann*, 104 N. Y. Misc. 46, 171 N. Y. Supp. 193; *Ohio River Power Co. v. Steubenville*, 99 Ohio St. 421, 124 N. E. 246; *Cincinnati v. Public Utilities Commission*, 98

Ohio St. 320, 3 A. L. R. 705, 121 N. E. 688; *Interurban Railway & Terminal Co. v. Public Utilities Commission*, 98 Ohio St. 287, 3 A. L. R. 696, 120 N. E. 831; *Virginia-Western Power Co. v. Com. ex rel. City of Clifton Forge*, 125 Va. 469, 99 S. E. 723. See also *Quinby v. Public Service Commission*, 223 N. Y. 244, 3 A. L. R. 685, 119 N. E. 433.

In some states the public service commission statute expressly provides that the commission shall have no power to change rates fixed by contract between a municipality and a public utility. See *City of Mobile v. Mobile Elec. Co.*, 203 Ala. 574, 84 So. 816.

In Ohio, the public utilities commission cannot authorize a gas company to charge more than the rate fixed by contract between the company and the city. *Lima v. Public Utilities Commission*, 100 Ohio St. 416, 126 N. E. 318.

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are many late decisions, as to some of which it is difficult if not impossible to ascertain the basis for the ruling, holding that rate contracts contained in municipal franchises are not inviolable, and that the rates so fixed may be subsequently changed by the state through its legislature or public service commission.³³ Some of these decisions giving the state the power to regulate rates already fixed by contract are based on express constitutional or statutory provisions antedating the rate contract.³⁴ Other deci-

of New York has no power to regulate rates where fixed by a contract between a city and the corporation. *Westinghouse Elec. & Mfg. Co. v. Binghampton Ry. Co.*, 255 Fed. 378.

³³ *State ex rel. Swearingen v. Railroad Com'rs*, — Fla. —, 84 So. 444; *State ex rel. Triay v. Burr*, — Fla. —, 84 So. 61; *Public Service Commission v. Girtton*, — Ind. —, 128 N. E. 690; *Fulton v. Public Service Commission*, 275 Mo. 67, 204 S. W. 386, overruling *State v. Laclede Gaslight Co.*, 102 Mo. 472, 22 Am. St. Rep. 789, 14 S. W. 974, 15 S. W. 383; *Public Service Commission v. Pavilion Natural Gas Co.*, 111 N. Y. Misc. 692, 182 N. Y. Supp. 55; *Warsaw v. Pavilion Natural Gas Co.*, 111 N. Y. Misc. 565, 182 N. Y. Supp. 73; *International R. Co. v. Public Service Commission*, 106 N. Y. Misc. 293, 174 N. Y. Supp. 403; *Murray City v. Utah Light & Traction Co.*, — Utah —, 191 Pac. 421. See also *City of Niagara Falls v. Public Service Commission for Second Dist.*, 108 N. Y. Misc. 567, 177 N. Y. Supp. 861.

In Missouri, rates of street car companies as fixed by the franchise are nevertheless subject to change by the public service commission. *Kansas City v. Public Service Commission*, 276 Mo. 539, 210 S. W. 381; *St. Louis v. Public*

Service Commission, 276 Mo. 509, 207 S. W. 799.

In Oregon, the state, through its public service commission, may increase the fares of a street car company, above the maximum fixed by the franchise. *Portland v. Public Service Commission*, 89 Ore. 325, 173 Pac. 1178.

The rule in Pennsylvania is that "where contracts fixing a rate 'unlimited' in time have heretofore been entered into by public service companies, the state has the right, through the Public Service Commission, notwithstanding the contract, to inquire into and adjust the rate to a reasonable basis." *St. Clair Borough v. Tamaqua & P. Elec. R. Co.*, 259 Pa. 462, 5 A. L. R. 20, 103 Atl. 287.

A franchise contract between a city and a power company fixing the price to be paid by the city for hydrants involves rate making so as to be subject to change by the state under the Oregon decisions. *City of Hillsboro v. Public Service Commission of Oregon*, — Ore. —, 187 Pac. 617.

³⁴ Of course a franchise contract fixing rates is not binding on a public service commission where made after the enactment of a statute giving such commission the power to decrease or increase the rates. *People ex rel.*

sions are based on the theory that power to regulate rates is a part of the police power and can never be delegated so as to deprive the state of its exercise.³⁵ In Arkansas, it is held

City of New York v. Nixon, — N. Y. —, 128 N. E. 245, rev'g 190 N. Y. App. Div. 612, 180 N. Y. Supp. 130, which aff'd 109 N. Y. Misc. 7, 179 N. Y. Supp. 82.

If the duty of fixing maximum rates is imposed on the legislature by the constitution, and it appoints a public service commission for that purpose, it seems that a municipality cannot thereafter make a contract fixing rates except subject to the power of the commission to change the rates. *Salt Lake City v. Utah Light & Traction Co.*, 52 Utah 210, 173 Pac. 556.

In Georgia, statutes permit the railroad commission to lower or increase rates of public service companies, although made the subject of a franchise contract entered into since the enactment of such statutes. *Atlanta v. Georgia Railway & Power Co.*, 149 Ga. 411, 100 S. E. 442.

In New York, a recent decision of the Court of Appeals enumerates certain classes of franchises as to which the public service commission has jurisdiction to regulate rates, including (1) all franchises granted directly by the legislature, (2) all franchises granted by municipal authorities prior to Jan. 1, 1875, and (3) all franchises granted by municipalities subsequent to the passage of the Public Service Commissions Law in 1907. *People ex rel. Garrison v. Nixon*, — N. Y. —, 128 N. E. 255, aff'g 191 N. Y. App. Div. 945, 181 N. Y. Supp. 949.

³⁵ In Pennsylvania, it seems that

no franchise contract as to rates is binding on the state, on the theory that the police power of regulating rates cannot be delegated so as to prevent its exercise by the state at any time. *Scran-ton v. Public Service Commission*, — Pa. —, 110 Atl. 775.

In Pennsylvania, franchise rates are deemed subject to change by the state because of the constitutional provision that "the exercise of the police power of the state shall never be abridged or so construed as to permit corporations to conduct their business in such manner as to infringe the equal rights of individuals or the general well being of the state." *McKeesport v. Pittsburgh Rys. Co.*, 72 Pa. Super. Ct. 435; *Borough of Wilkinsburg v. Public Service Commission*, 72 Pa. Super. Ct. 423.

In Michigan it is held that "the legislature cannot, by a grant of power to the several municipalities of the state, divest itself of the right to reassume and itself exercise such powers as are granted it in that behalf under the Constitution, among which is this power to fix reasonable rates," and that this rule enables the legislature to increase rates fixed by a municipal franchise contract. *Attorney General v. Detroit United Ry.*, 210 Mich. 227, 177 N. W. 726, 1023.

In Tennessee, on the theory that governmental powers of the state cannot be bargained away, rates may be changed by the public service commission regardless of

that the power of the state to regulate rates is an attribute of sovereignty which cannot be contracted away by the state or by a municipality so as to prevent future regulation by the state.³⁶

A provision in a street railway franchise requiring sale of half-fare tickets to certain persons at certain hours is not, in Iowa, within the constitutional protection against impairment of contracts, but may be changed by the legislature.³⁷

An ordinance compelling a street car company to carry passengers on continuous trips over franchise lines to and over non-franchise lines, and vice versa, for a fare no greater than its franchises entitle it to charge upon the former alone, impairs the obligation of the franchise contracts.³⁸

As evidencing the trend of the decisions, it was recently held in New York that while a contract for a supply of gas to a municipality itself may constitute an inviolable contract, yet a franchise fixing the rates for gas supplied to inhabitants is not a contract "beyond the inherent police power of the legislature to modify for the public welfare."³⁹ But in West Virginia it is held that there is no difference between municipal power to make inviolable rate contracts for itself and to make such contracts for its inhabitants.⁴⁰

A municipal corporation, an agency of the state, is not protected, it seems, on the theory of impairment of contract as to rates made by a franchise, from a change of rates as against its own creator, the state.⁴¹

An important question has arisen in connection with the late municipal franchise contracts. *Y. App. Div. 175, 162 N. Y. Supp. 581.*
Memphis v. Enloe, 141 Tenn. 618, 214 S. W. 71.

³⁶ *City of Camden v. Arkansas Light & Power Co.*, — Ark. —, 224 S. W. 444.

³⁷ *Dubuque Elec. Co. v. Dubuque*, 260 Fed. 353, 10 A. L. R. 495.

³⁸ *Detroit United Ry. v. City of Detroit*, 248 U. S. 429, 63 L. Ed. 341.

³⁹ *People ex rel. Village of South Glens Falls v. Public Service Commission*, 225 N. Y. 216, 121 N. E. 777. See also *Kings County Lighting Co. v. New York*, 176 N.

⁴⁰ *Charleston v. Public Service Commission*, — W. Va. —, 103 S. E. 673.

⁴¹ *Collingswood Sewerage Co. v. Collingswood*, 91 N. J. L. 20, 102 Atl. 901.

That a franchise contract as to rates may be changed by the state by increasing the rate, although the municipality objects, is the ruling, it seems, in some states. In *re* *Petition for Increase of Street Car Fares*, 179 N. C. 151, 101 S. E. 619.

world war as to whether public service corporations bound by contract not to exceed a maximum rate were entitled to relief from the contract and to an increase of rates because of the high cost of everything due to the war and the resulting inability to operate successfully under the contract rate. Some of the state courts held that the contract was abrogated by the change of conditions or that relief was authorized on other grounds,⁴² but the Supreme Court of the United States has held that a street railroad company is not released from its franchise contract as to maximum fares by conditions following the world war and resulting in a great increase of wages by award of the War Labor Board, where it is not, and cannot be, shown that the performance of the contract taking all the years of the term together, will prove unremunerative.⁴³ There are several other federal decisions refusing relief to such corporations, some of them expressly relying on the street railway decision of the United States Supreme Court.⁴⁴ So there are decisions in the state courts refusing relief.⁴⁵

⁴² See *Bronx Gas & Electric Co. v. Public Service Commission*, 190 N. Y. App. Div. 13, 180 N. Y. Supp. 38.

Rates of a street car company may be increased because of abnormal conditions due to the war. In *re Lincoln Traction Co.*, 103 Neb. 229, 171 N. W. 192.

In Indiana, the public service commission may, by statute, increase street railway fares temporarily, in case of an "emergency," such as the late war, without regard to any rate fixed by franchise. *State ex rel. Indianapolis Traction & Terminal Co. v. Lewis*, 187 Ind. 564, 120 N. E. 129.

Increase of street car fare because of war, validity of repeal of increase because of change of conditions, see *Houston Elec. Co. v. Houston*, — Tex. Civ. App. —, 212 S. W. 198.

⁴³ *Columbus Railway, Power & Light Co. v. City of Columbus*, 249

U. S. 399, 63 L. Ed. 669, 6 A. L. R. 1648, aff'g 253 Fed. 499.

This decision of the United States Supreme Court is annotated at length in a recent note in 6 *American Law Reports* 1659, under the title of "Right of public service corporation to judicial relief from contract rates which have become inadequate."

⁴⁴ *Knoxville Gas Co. v. Knoxville*, 261 Fed. 283; *Muscatine Lighting Co. v. Muscatine*, 256 Fed. 929; *Burr v. Columbus*, 256 Fed. 261; *City of Moorehead v. Union Light, Heat & Power Co.*, 255 Fed. 920; *Knoxville Gas Co. v. Knoxville*, 253 Fed. 217.

A public service company is not excused from complying with the franchise rate of fare because increased wages were fixed at a confiscatory rate by the War Labor Board. *Burr v. Columbus*, 256 Fed. 261.

⁴⁵ *Miami Gas Co. v. Highleyman*, 77 Fla. 523, 81 So. 775; *Lenawee*

§ 4490. — As dependent upon power of municipality to make contract as to rates. Of course if the municipality has no power to contract as to rates, then rates fixed by the franchise may be increased or decreased by the state.⁴⁶ A municipality cannot make a contract as to rates, so as to prevent the state from changing the rates, unless the power to make such a contract has been clearly delegated to the municipality.⁴⁷ In determining

County Gas & Electric Co. v. Adrian, 209 Mich. 52, 176 N. W. 590.

Franchise rates cannot be interfered with on the ground that they will result in bankruptcy of the utility. Lonoke v. W. Y. Bransford & Son, 141 Ark. 18, 216 S. W. 38.

⁴⁶ Meridian Light & Railway Co. v. City of Meridian, 265 Fed. 765; City of Sapulpa v. Oklahoma Natural Gas Co., — Okla. —, 192 Pac. 224; City of Hillsboro v. Public Service Commission, — Ore. —, 192 Pac. 390.

In Idaho, municipalities have no power to contract as to rates so as to bind the state. Sandpoint Water & Light Co. v. City of Sandpoint, 31 Idaho 498, L. R. A. 1918 F 1106, 173 Pac. 972.

⁴⁷ Knoxville Gas Co. v. Knoxville, 261 Fed. 283; Columbus Railway, Power & Light Co. v. Columbus, 253 Fed. 499; State ex rel. Triay v. Burr, — Fla. —, 84 So. 61; Sandpoint Water & Light Co. v. City of Sandpoint, 31 Idaho 498, L. R. A. 1918 F 1106, 173 Pac. 972; Ottumwa Railway & Light Co. v. Ottumwa, — Iowa —, 178 N. W. 905; In re Searsport Water Co., 118 Me. 382, 108 Atl. 452; In re Guilford Water Co.'s Service Rates, 118 Me. 367, 108 Atl. 446; Traverse City v. Michigan Railroad Commission, 202 Mich. 575, 168 N. W. 481; State

ex rel. City of Billings v. Billings Gas Co., 55 Mont. 102, 173 Pac. 799; Charleston v. Public Service Commission, — W. Va. —, 103 S. E. 673. See also Virginia-Western Power Co. v. Com. ex rel. City of Clifton Forge, 125 Va. 469, 99 S. E. 723.

In Illinois, the legislature has never conferred on any municipality power to make inviolable rates for a public utility. Chicago Rys. Co. v. Chicago, 292 Ill. 190, 126 N. E. 585.

Municipalities in Illinois cannot make binding contracts for street car fares for a term of years, so as to prevent change of the rates by the state. State Public Utilities Commission v. Quincy, 290 Ill. 360, 125 N. E. 374.

In Missouri it is now held that because of the constitutional provision that the exercise of the state police power shall never be abridged, the legislature has no power to delegate to a municipality the power to make a contract as to rates which will prevent regulation of such rates by the public service commission. State ex rel. City of Sedalia v. Public Service Commission, 275 Mo. 201, 204 S. W. 497.

In Ohio, the power is delegated to cities to contract as to maximum rates on granting a street franchise to a street railway company. Columbus Railway, Power

whether power is granted a city to contract as to rates, the courts "incline to the natural and usual construction of the words of a statute."⁴⁸ Where the state has regulated rates, a city has no power to thereafter contract as to rates so as to preclude the state from altering such rates.⁴⁹ Exclusive power conferred by the constitution on cities to grant consent to use of their streets by street car companies does not include power to contract as to fares so as not to be subject to state regulation.⁵⁰ It has been held that the power of a city to fix conditions on granting a street franchise does not include power to contract as to rates so as to bind the state;⁵¹ but it is also held that statutory power to prescribe reasonable regulations for a gas company includes authority of a city to contract as to gas rates.⁵² Under a Ten-

& Light Co. v. Columbus, 253 Fed. 499.

Under the Texas Constitution forbidding irrevocable grants of special immunities, a Texas city cannot make an irrevocable contract fixing rates. San Antonio Public Service Co. v. San Antonio, 257 Fed. 467.

In Washington, a city cannot, by contract, fix a rate which the public service commission cannot increase. State ex rel. City of Seattle v. Public Service Commission, 103 Wash. 72, 173 Pac. 737.

Public policy forbids inviolable rate contracts between a municipality and a public service company, in the absence of an unmistakable declaration by the legislature that such contracts do not offend that policy. Ottumwa Railway & Light Co. v. Ottumwa, — Iowa —, 178 N. W. 905.

⁴⁸ Omaha Gas Co. v. Omaha, 249 Fed. 350.

⁴⁹ Westinghouse Elec. & Mfg. Co. v. Binghampton Ry. Co., 255 Fed. 378.

Where the legislature has fixed a rate of fare to be charged by

railroads and has authorized them to use public streets, a city, on granting consent to use streets, has no power to contract as to rates different from those fixed by the statute. See *People ex rel. New York, W. & B. Ry. Co. v. Public Service Commission*, — N. Y. App. Div. —, 183 N. Y. Supp. 473.

⁵⁰ St. Louis v. Public Service Commission, 276 Mo. 509, 207 S. W. 799.

⁵¹ Salt Lake City v. Utah Light & Traction Co., 52 Utah 210, 173 Pac. 556. Contra, see *Georgia Railway & Power Co. v. Railroad Commission*, 149 Ga. 1, 5 A. L. R. 1, 98 S. E. 696.

Statutory power conferred on a city to consent to a street railroad on its streets upon such terms and conditions as the city deems best, does not confer the right to contract for rates of fare so as to be free from legislative control. *Chicago Rys. Co. v. Chicago*, 292 Ill. 190, 126 N. E. 585.

⁵² Lenawee County Gas & Electric Co. v. Adrian, 209 Mich. 52, 176 N. W. 590.

nessee statute providing that a gas company shall not use city streets "until the consent" of the city is obtained "and an ordinance shall have been passed prescribing the terms on which the same may be done," a city has authority by ordinance to contract by fixing maximum rates.⁵³ Permission given a city to fix rates by contract may be merely a license revocable at the will of the legislature.⁵⁴

The right of a city to contract as to maximum gas rates, on granting a franchise, where conferred by statute, is not impaired by another statute providing that gas companies shall charge reasonable rates not in excess of a specified rate.⁵⁵

A constitutional provision that the state shall never surrender the right to fix charges of public service corporations has been held not to prevent a city making an irrevocable contract as to rates on granting a franchise.⁵⁶

Statutes in Iowa preclude cities from making any contract fixing permanent rates of particular public service companies, but not including street car companies; but such statutes are not to be construed as authorizing such contracts in case of street car companies merely because they are omitted from the statute.⁵⁷

Where power exists to make a contract as to rates, it may be made for a reasonable period, such as 25 years.⁵⁸ A franchise contract as to rates, even if invalid so far as perpetual, will be enforced for the thirty years which is the statutory limit for franchises.⁵⁹

§ 4493. — Franchise as constituting an actual contract as to rates. Of course there is no franchise contract as to rates, unless the franchise ordinance is accepted.⁶⁰

⁵³ Knoxville Gas Co. v. Knoxville, 253 Fed. 217.

⁵⁴ In re Guilford Water Co.'s Service Rates, 118 Me. 367, 108 Atl. 446.

⁵⁵ Knoxville Gas Co. v. Knoxville, 253 Fed. 217.

⁵⁶ Virginia-Western Power Co. v. Com. ex rel. City of Clifton Forge, 125 Va. 469, 99 S. E. 723.

⁵⁷ Ottumwa Railway & Light Co. v. Ottumwa, — Iowa —, 178 N.

W. 905; Ottumwa Railway & Light Co. v. Ottumwa, — Iowa —, 173 N. W. 270.

⁵⁸ Omaha Gas Co. v. Omaha, 249 Fed. 350.

⁵⁹ Mobile Elec. Co. v. City of Mobile, 201 Ala. 607, 79 So. 39, recognizing a conflict in the decisions.

⁶⁰ Oak Harbor v. Public Utilities Commission, 99 Ohio St. 275, 124 N. E. 158; Washington v. Public

Where a statute, at the time a railroad company was created, fixes maximum rates for railroads, the statute becomes a part of the franchise so that the company cannot exceed such rate because the company cannot profitably operate under such rates.⁶¹ In Michigan, it is held that a statute providing that "the rates * * * established by agreement * * * shall not be increased without consent of such [municipal] authorities," is not a contract between the state and the municipality, but is merely a delegation of state power which the legislature may reassume and itself exercise.⁶²

§ 4494. — Power of municipality to change rate as distinguished from power of state. A franchise contract as to rates cannot be abrogated by either party.⁶³ A contract as to rates between a municipality and a company may bind both parties and yet not be binding on the state which may change the rates.⁶⁴

§ 4495. — Right of corporation or commission to increase rates. Rates as fixed by a franchise contract cannot be violated by the public service corporation where the state does not authorize or consent to the change.⁶⁵ A gas company cannot itself increase its rates above the franchise rate although power exists to apply to the public service commission for such an increase.⁶⁶ It cannot be claimed that an ordinance fixing maximum rates is not binding on the city, and hence not on the public service company, because the present or any succeeding law-making

Utilities Commission, 99 Ohio St. 70, 124 N. E. 46.

⁶¹ *Charleston-Isle of Palms Traction Co. v. Shealy*, 266 Fed. 406, following *Columbus Ry. v. Columbus*, 249 U. S. 399, 63 L. Ed. 669.

⁶² *Attorney General v. Detroit United Ry.*, 210 Mich. 227, 177 N. W. 726, 1023.

⁶³ *Hillsdale Gaslight Co. v. Hillsdale*, 258 Fed. 485.

⁶⁴ *In re Guilford Water Co.'s Service Rates*, 118 Me. 367, 108 Atl. 446; *Salt Lake City v. Utah Light & Traction Co.*, 52 Utah 210, 173 Pac. 556.

A binding contract as to rates may exist between a municipality and a corporation, pursuant to a franchise, without any restriction on the power of the state to regulate rates. *Atlantic Coast Elec. R. Co. v. Board of Public Utility Com'rs*, 92 N. J. L. 168, 104 Atl. 218. See dissenting opinion of Justice White.

⁶⁵ *State ex rel. Ellertsen v. Home Telephone & Telegraph Co.*, 102 Wash. 196, 172 Pac. 899.

⁶⁶ *Village of Freeport v. Nassau & Suffolk Lighting Co.*, 111 N. Y. Misc. 671, 181 N. Y. Supp. 830.

power may change or repeal the ordinance outright, since the contract as to rates relates to business or proprietary powers, so as to be not repealable, as distinguished from governmental powers.⁶⁷

§ 4496. — Regulations as impairing contracts between corporation and third person. Rates may be regulated by the state although superseding lower rates agreed on in an existing time contract between the company and a consumer.⁶⁸ A common carrier cannot, by making contracts for future transportation or by mortgaging its property or pledging its income, prevent state regulation of rates.⁶⁹ Power of the state to change railroad rates precludes an irrevocable contract between an owner of land and a railroad company as to rates in consideration of a grant of a right of way.⁷⁰ But a contract between a consumer and a public service company as to rates is binding on the company so far as to prevent it, of its own motion and without the consent of its customer or action on the part of the public service commission, from increasing the rate.⁷¹

§ 4497. — Waiver or abandonment of contract rights. A franchise contract may be modified by mutual consent of the municipality and the public service company, by raising rates, so that property owners or patrons cannot object.⁷² Where a city fixed the fare of a street railroad operated by animal power

⁶⁷ Knoxville Gas Co. v. Knoxville, 253 Fed. 217, 223.

⁶⁸ Union Dry Goods Co. v. Georgia Public Service Corporation, 248 U. S. 372, 63 L. Ed. 309, 9 A. L. R. 1420, aff'g 145 Ga. 658, 89 S. E. 779; Ohio & Colorado Smelting & Refining Co. v. Public Utilities Commission, — Colo. —, 187 Pac. 1082; Public Service Commission v. Girton, — Ind. —, 128 N. E. 690; Edison Storage Battery Co. v. Board of Public Utility Com'rs, 93 N. J. L. 301, 108 Atl. 247; Leiper v. Baltimore & P. R. Co., 262 Pa. 328, 105 Atl. 551.

⁶⁹ Producers Transp. Co. v. Rail-

road Commission, 251 U. S. 228, 63 L. Ed. 239, aff'g 176 Cal. 499, 169 Pac. 59.

⁷⁰ Schaper v. Cleveland & E. R. Co., 265 Pa. 109, 108 Atl. 407.

⁷¹ Rutland Railway, Light & Power Co. v. Burditt Bros., — Vt. —, 111 Atl. 582.

⁷² Arkansas Light & Power Co. v. Cooley, 138 Ark. 390, 211 S. W. 664; Phelps v. Logan Natural Gas & Fuel Co., — Ohio St. —, 128 N. E. 58, citing 4 McQuillin Mun. Corp. § 1763. See also Robertson v. Wilmington & P. Traction Co., 7 Boyce (30 Del.) 155, 104 Atl. 839.

at five cents, consent to electrification of the roads cancels the limitation as to fare.⁷³

A lessee of a railroad cannot waive or impair any contract right of the lessor to charge a certain fare.⁷⁴

D. Discrimination in Rates

§ 4498. General considerations. The objection that a state rate discriminates between shippers is not available to a carrier.⁷⁵ A gas company may place its patrons in different classes, and base rates upon the varying cost of the service rendered.⁷⁶

§ 4507. Free or reduced rates for particular passengers—Six tickets for a quarter. A regulation fixing a seven cent street car fare on sales of five tickets, and otherwise a ten cent fare, is reasonable.⁷⁷

§ 4512. — Requiring reduced or free transportation for soldiers, police officers, detectives, etc.⁷⁸

§ 4513. — Forbidding issuance of free passes. A state may forbid free passes by public service companies,⁷⁹ and may render illegal and unenforceable a pass given to a resident for use over an interstate bridge.⁸⁰

E. Reasonableness of Rates Fixed by Law

§ 4517. General rules. A rate may be enjoined, although not confiscatory, where unreasonable and unjust.⁸¹ A reasonable

⁷³ Westinghouse Elec. & Mfg. Co. v. Binghamton Ry. Co., 255 Fed. 378.

⁷⁴ People ex rel. Brooklyn City R. Co. v. Nixon, 193 N. Y. App. Div. 746, 184 N. Y. Supp. 369.

⁷⁵ Arkadelphia Milling Co. v. St. Louis Southwestern R. Co., 249 U. S. 134, 63 L. Ed. 517.

⁷⁶ Clarksburg Light & Heat Co. v. Public Service Commission, — W. Va. —, 100 S. E. 551.

⁷⁷ Donham v. Public Service Com'rs, 232 Mass. 309, 122 N. E. 397. See also Fall River v. Public

Service Com'rs, 232 Mass. 329, 122 N. E. 406.

⁷⁸ Construction of ordinance requiring free transportation of police officers when in uniform, see Montgomery Light & Traction Co. v. Avant, 202 Ala. 404, 3 A. L. R. 384, 80 So. 497.

⁷⁹ Shrader v. Steubenville, E. L. & B. Val. Traction Co., — W. Va. —, 99 S. E. 207.

⁸⁰ Shrader v. Steubenville, E. L. & B. Val. Traction Co., — W. Va. —, 99 S. E. 207.

⁸¹ Houston Elec. Co. v. Houston,

rate is one which yields a fair return on the value of the property necessarily employed over and above expenses and depreciation.⁸² The income of a gas plant in an abnormal year, such as 1918, although not an adequate return on the investment, does not show the rates to be confiscatory.⁸³ Rates should be as low as possible and yet sufficient to induce the investment of capital.⁸⁴ A rate may afterwards become confiscatory although not so when fixed.⁸⁵ In the absence of contract, a public service company cannot be required to operate where the rates fixed by the state will not pay expenses.⁸⁶

A just and reasonable rate "is necessarily a question of sound business judgment rather than one of legal formula, and must often be tentative, since exact results cannot be foretold."⁸⁷

§ 4518. Matters to be considered. It is no ground for refusing to increase suburban railway rates, in excess of the rates fixed by the franchise, that many persons have built homes in suburbs and along the road in reliance on such rates.⁸⁸ Where "the corporate organization and affairs of one railroad company are controlled and dominated by another railroad company through ownership of stock or lease, the roads must be regarded as identical for the purpose of rate making."⁸⁹ Earnings of subsidiary companies must be accurately ascertained and accounted for the same as other earnings of the parent company, for the purpose of rate regulation of the latter.⁹⁰

— Tex. Civ. App. —, 212 S. W. 198.

Gas rate as confiscatory, see *Jamaica Gaslight Co. v. Nixon*, 110 N. Y. Misc. 500, 181 N. Y. Supp. 623.

⁸² *Milwaukee Elec. Railway & Light Co. v. Railroad Commission*, 169 Wis. 421, 172 N. W. 746.

⁸³ *Kings County Lighting Co. v. Lewis*, 110 N. Y. Misc. 204, 180 N. Y. Supp. 570.

⁸⁴ *State Public Utilities Commission v. Springfield Gas & Electric Co.*, 291 Ill. 209, 125 N. E. 891.

⁸⁵ *Municipal Gas Co. v. Public Service Commission*, 225 N. Y. 89, 121 N. E. 772.

⁸⁶ *Charleston-Isle of Palms Traction Co. v. Shealy*, 266 Fed. 406, and see § 4423, *supra*.

⁸⁷ *State Public Utilities Commission v. Springfield Gas & Electric Co.*, 291 Ill. 209, 125 N. E. 891.

⁸⁸ *Salt Lake City v. Utah Light & Traction Co.*, 52 Utah 210, 173 Pac. 556.

⁸⁹ *Pontiac, O. & N. R. Co. v. Michigan Railroad Commission*, 203 Mich. 258, 168 N. W. 927.

⁹⁰ *In re Lincoln Traction Co.*, 103 Neb. 229, 171 N. W. 192.

§ 4526. Reasonableness of return as a whole. Rates cannot be complained of where a carrier receives, in the aggregate, fair remuneration, although rates on part of its business are not remunerative.⁹¹ The true test of the reasonableness of a rate is its effect on the entire system operated by the public utility, and not whether a particular part thereof is operated at a profit or loss under the prescribed rate.⁹² That the cost of supplying gas to small consumers is greatly in excess of the rate allowed does not necessarily show the rates as a whole to be unjust.⁹³

§ 4527. Reasonableness as affected by comparison with rates of other companies or in other localities. Rates allowed in other similar cities may be considered but are not controlling.⁹⁴

§ 4529. Methods of valuation in general.⁹⁵ To ascertain value, the "commission is not bound to adopt any one method to the exclusion of all others."⁹⁶ Exchange value, measured by return, should not be considered in fixing rates.⁹⁷

⁹¹ *Vandalia R. Co. v. Schnull*, 188 Ind. 87, 122 N. E. 225.

In fixing rates, loss on a suburban line as compensated by profits from the city line, see *Inhabitants of Trenton v. Trenton & Mercer County Traction Co.*, 92 N. J. L. 61, 105 Atl. 136.

⁹² *Milwaukee Elec. Railway & Light Co. v. Railroad Commission*, — Wis. —, 177 N. W. 25, applying rule to company operating street and suburban railways as one system.

⁹³ *State Public Utilities Commission v. Springfield Gas & Electric Co.*, 291 Ill. 209, 125 N. E. 891.

⁹⁴ *In re Lincoln Traction Co.*, 103 Neb. 229, 171 N. W. 192.

⁹⁵ Valuation for rate making, see generally *Ohio & Colorado Smelting & Refining Co. v. Public Utilities Commission*, — Colo. —, 187 Pac. 1082.

Mode of determining valuation of intercounty power lines owned by power company, see *State v. State Board of Equalization*, 56 Mont. 413, 185 Pac. 708, 186 Pac. 697.

Valuation of water plant, including water-bearing land, for rate purposes, see *Union Hollywood Water Co. v. Los Angeles*, 178 Cal. 206, 172 Pac. 983.

Valuation of property of telephone company for rate purposes, see *Lima Telephone & Telegraph Co. v. Public Utilities Commission*, 98 Ohio St. 110, 120 N. E. 330.

⁹⁶ *Ben Avon v. Ohio Valley Water Co.*, 260 Pa. 289, 103 Atl. 744.

⁹⁷ *State Public Utilities Commission v. Springfield Gas & Electric Co.*, 291 Ill. 209, 125 N. E. 891.

§ 4530. Original cost as test. Original cost less depreciation should not be the sole test in determining value.⁹⁸ If the property has increased in value over the cost price, the rate should be based on such valuation.⁹⁹ Amounts paid by a street railway company in purchasing separate railways of which its system is composed need not be allowed, in valuing property for rate purposes.¹

§ 4531. Present value as test—General rule. The fair present value of the property is the basis on which a fair return should be paid.² Every part of a railroad system within the state must be included in determining whether a rate is confiscatory; and hence sleeping car, parlor car, and dining car services should be taken into consideration in determining whether a railroad rate is confiscatory.³

Where the value of a public utility's property has increased so enormously since its acquisition as to render a rate permitting a reasonable return upon such increased value unjust to the public, such a rate will not be allowed.⁴

§ 4532. — What constitutes "value" in general. Interest on land is not an element of value.⁵

§ 4535. — Value of property not used. Plants not used are not to be considered in valuing a water plant.⁶

§ 4537. — Value as "going concern" as item. "Going concern" value should be considered.⁷ "Going value" should not

⁹⁸ State Public Utilities Commission v. Springfield Gas & Electric Co., 291 Ill. 209, 125 N. E. 891; City of Detroit v. Michigan Railroad Commission, 209 Mich. 395, 177 N. W. 306.

⁹⁹ Houston Elec. Co. v. City of Houston, 265 Fed. 360.

¹ Milwaukee Elec. Railway & Light Co. v. Railroad Commission, 169 Wis. 421, 172 N. W. 746.

² Kings County Lighting Co. v. Lewis, 110 N. Y. Misc. 204, 180 N. Y. Supp. 570.

³ Groesbeck v. Duluth, S. S. &

A. R. Co., 250 U. S. 607, 63 L. Ed. 1167.

⁴ State Public Utilities Commission v. Springfield Gas & Electric Co., 291 Ill. 209, 125 N. E. 891.

⁵ New York Interurban Water Co. v. Mt. Vernon, 110 N. Y. Misc. 281, 180 N. Y. Supp. 304.

⁶ New York Interurban Water Co. v. Mt. Vernon, 110 N. Y. Misc. 281, 180 N. Y. Supp. 304.

⁷ Denver v. Denver Union Water Co., 246 U. S. 178, 191, 62 L. Ed. 649. See also Kings County Lighting Co. v. Lewis, 110 N. Y. Misc.

be separately allowed merely because of an overissue of security when the water company first took over its plant from another company.⁸ Restriction of "going value" on the theory that past earnings were excessive, is improper, in the absence of any clear evidence that they were excessive.⁹ The courts will not substitute their judgment for that of the public service commission as to the valuation put on "going value."¹⁰

§ 4538. — Franchise as item of value. The franchise is not separately valued, in New York, in fixing rates.¹¹

§ 4539. — Good will as item of value. Good will is not considered as a distinct element of value.¹²

§ 4541. — Deduction for depreciation. Depreciation must be taken into consideration.¹³ In figuring rates, a ferry company may set aside a reasonable amount from gross income to make good the depreciation.¹⁴

§ 4543. Cost of reproduction as test—In general. Cost of reproduction less depreciation is not the only basis for determining value;¹⁵ and cost of reproduction at a time of abnormally high prices is not a proper method of valuation.¹⁶

§ 4546. Operating expenses—In general.¹⁷ Operating expenses as charged by the utility cannot be ignored by the com-

204, 180 N. Y. Supp. 570; Ben Avon v. Ohio Valley Water Co., 260 Pa. 289, 103 Atl. 744.

⁸ New York Interurban Water Co. v. Mt. Vernon, 110 N. Y. Misc. 281, 180 N. Y. Supp. 304.

⁹ Lincoln Gas & Electric Light Co. v. City of Lincoln, 250 U. S. 256, 63 L. Ed. 968.

¹⁰ State Public Utilities Commission v. Springfield Gas & Electric Co., 291 Ill. 209, 125 N. E. 891.

¹¹ Bronx Gas & Electric Co. v. Public Service Commission, 190 N. Y. App. Div. 13, 180 N. Y. Supp. 38.

¹² In re Lincoln Traction Co., 103 Neb. 229, 171 N. W. 192.

¹³ Kings County Lighting Co. v. Lewis, 110 N. Y. Misc. 204, 180 N. Y. Supp. 570.

¹⁴ Port Richmond & Bergen Point Ferry Co. v. Board Chosen Freeholders of Hudson County, 264 Fed. 998.

¹⁵ State Public Utilities Commission ex rel. City of Springfield v. Springfield Gas & Electric Co., 291 Ill. 209, 125 N. E. 891.

¹⁶ Kings County Lighting Co. v. Lewis, 110 N. Y. Misc. 204, 180 N. Y. Supp. 570.

¹⁷ What are operating expenses, see Kings County Lighting Co. v.

mission unless there is an abuse of discretion, as to the amounts, by the corporate officers.¹⁸ Average operating expenses of like companies in other cities similarly situated may be considered by the commission.¹⁹ Operating expenses do not include legal expenses to defeat the rate law,²⁰ nor a gratuity paid a retired officer,²¹ nor the federal income tax.²² New pipe lines of a natural gas company are an item of investment and not an expense of operation.²³

§ 4547. — Depreciation fund. Where the life of a gas company is determined by the life of its gas fields, there must be allowed, in valuation for fixing rates, an item sufficient to amortize the plant within the probable life of the gas fields.²⁴ Where a railroad serving a logging territory will be valuable only as junk when the timber is exhausted, rates should give not only a reasonable return on the money invested plus interest charges but also provide for amortization of the plant.²⁵

§ 4548. Rate of return to which corporation entitled. The rate of return is governed by the conditions existing in the community, including returns upon investments in similar or other securities.²⁶ What would have been a proper rate of return for capital invested in gas plants and similar utilities before the world war furnishes no safe criterion for the present or for the future.²⁷ A rate yielding as much as six per cent may be re-

Lewis, 110 N. Y. Misc. 204, 180 N. Y. Supp. 570, where many items involved.

¹⁸ State Public Utilities Commission v. Springfield Gas & Electric Co., 291 Ill. 209, 125 N. E. 891.

¹⁹ State Public Utilities Commission v. Springfield Gas & Electric Co., 291 Ill. 209, 125 N. E. 891.

²⁰ Kings County Lighting Co. v. Lewis, 110 N. Y. Misc. 204, 180 N. Y. Supp. 570.

²¹ Kings County Lighting Co. v. Lewis, 110 N. Y. Misc. 204, 180 N. Y. Supp. 570.

²² Jamaica Gaslight Co. v.

Nixon, 110 N. Y. Misc. 500, 181 N. Y. Supp. 623.

²³ Clarksburg Light & Heat Co. v. Public Service Commission, — W. Va. —, 100 S. E. 551.

²⁴ Clarksburg Light & Heat Co. v. Public Service Commission, — W. Va. —, 100 S. E. 551.

²⁵ Hammond Lumber Co. v. Public Service Commission, 96 Ore. 595, 189 Pac. 639.

²⁶ Houston Elec. Co. v. City of Houston, 265 Fed. 360; Henry L. Doherty & Co. v. Toledo Railways & Light Co., 254 Fed. 597.

²⁷ Lincoln Gas & Elec. Light Co. v. Lincoln, 250 U. S. 256, 63 L. Ed. 968.

garded as confiscatory where eight per cent is the lowest rate sought and generally obtained as a return upon capital invested in banking, merchandising, and other business in the vicinity.²⁸ A return of six per cent is not confiscatory, at least in case of a San Francisco water company, but a return of less than six was held confiscatory.²⁹ Water rates permitting a net return of ten per cent, after allowing an annual depreciation charge of three and one-half per cent, are not confiscatory.³⁰ A rate of seven and one-half per cent is a fair return in case of a street railroad.³¹ Seven per cent return allowed a gas company is not unreasonably low.³² Seven per cent is a proper rate of return for a water company.³³ A return of four and one-half per cent for a water company is unreasonable.³⁴

VIII. PROCEDURE CONNECTED WITH REGULATIONS AND REVIEW THEREOF

§ 4551. Procedure before commission—In general. An emergency increase of rates is provided for by some statutes, in which case the action of the public service commission is not to be judged nor tested by the same conditions as are its orders establishing permanent rates.³⁵ Temporary rates may be ordered by a public service commission where the necessity is apparent,³⁶ pending a full hearing.³⁷ Fixing of rates for

²⁸ Lincoln Gas & Elec. Light Co. v. Lincoln, 250 U. S. 256, 63 L. Ed. 968.

²⁹ Spring Valley Water Co. v. San Francisco, 252 Fed. 979.

³⁰ Van Dyke v. Geary, 244 U. S. 39, 61 L. Ed. 973, aff'g 218 Fed. 111.

³¹ Milwaukee Elec. Railway & Light Co. v. Railroad Commission, 169 Wis. 421, 172 N. W. 746.

³² State Public Utilities Commission v. Springfield Gas & Electric Co., 291 Ill. 209, 125 N. E. 891.

³³ New York Interurban Water Co. v. Mt. Vernon, 110 N. Y. Misc. 281, 180 N. Y. Supp. 304.

³⁴ Kent Water & Light Co. v. Public Utilities Commission, 97

Ohio St. 321, 119 N. E. 731.

³⁵ La Crosse v. Railroad Commission, — Wis. —, 178 N. W. 867.

³⁶ Muskogee Gas & Electric Co. v. State, — Okla. —, 186 Pac. 730. See also Omaha & C. B. St. R. Co. v. Nebraska State Ry. Commission, 103 Neb. 695, 173 N. W. 690.

Experimental period is proper. Donham v. Public Service Commission, 232 Mass. 309, 122 N. E. 397.

Experimental rate order, suspension of, see Charleston v. Public Service Commission, 83 W. Va. 718, 99 S. E. 63.

³⁷ Chicago Rys. Co. v. Chicago, 292 Ill. 190, 126 N. E. 585.

future business by a public service commission is legislative rather than judicial.³⁸

§ 4552. — Notice and hearing. In fixing rates, in some states, the commission may consider evidence not introduced at any hearing.³⁹ Fixing gas rates by comparison with rates in other cities, where the company is given no opportunity to distinguish between conditions, is improper, on the part of a public service commission.⁴⁰

Valuation is not always a prerequisite to an increase in rates by the state commission, as where an increase is shown to be necessary to meet increased costs.⁴¹

§ 4558. Review by courts in general—Power to review. Provisions conferring upon the supreme court of a state full jurisdiction to review the final orders of a public utilities commission conform to the constitutional requirement of opportunity for judicial review.⁴² If a statute does not authorize a review of orders of a public service commission fixing rates, and there is no method of review, it is unconstitutional.⁴³ Persons affected are entitled to a judicial review of orders of a public service commission, and if deprived thereof are protected by the due process of law provision.⁴⁴ Where confiscation is claimed as a result of rate regulations by a public service commission, the state must provide a fair opportunity for submitting that issue to a judicial tribunal for determination upon its own independent judgment as to both law and facts; otherwise the order is void as in conflict with the due process of law clause.⁴⁵

³⁸ *Missouri Southern R. Co. v. Public Service Commission*, 279 Mo. 484, 214 S. W. 379.

³⁹ *Atlanta v. Georgia Railway & Power Co.*, 149 Ga. 411, 100 S. E. 442.

⁴⁰ *People ex rel. Judge v. Public Service Commission*, 192 N. Y. App. Div. 837, 183 N. Y. Supp. 283.

⁴¹ Adding to street car fares just enough to meet the increased wages forced on the company by the War Labor Board is not objectionable and need not be based

on a valuation of the property. *O'Brien v. Board of Public Utility Com'rs*, 92 N. J. L. 44, 105 Atl. 132.

⁴² *Hocking Valley R. Co. v. Public Utilities Commission*, 100 Ohio St. 321, 126 N. E. 397.

⁴³ *Oklahoma Gin Co. v. State*, 252 U. S. 339, 64 L. Ed. 600; *Oklahoma Operating Co. v. Love*, 252 U. S. 331, 64 L. Ed. 596.

⁴⁴ *Florida East Coast Ry. Co. v. State*, — Fla. —, 83 So. 708.

⁴⁵ *Ohio Valley Water Co. v. Ben Avon Borough*, 253 U. S. 287, 64

Whether conditions imposed by a city on the use of streets by a street railroad company which has no franchise, are reasonable, is a subject of judicial inquiry.⁴⁶

Delay pending other proceedings is not laches precluding an attack on rates as confiscatory.⁴⁷

§ 4559. — Compliance with conditions precedent. The reasonableness of rules of a public service corporation is to be first determined by the public service commission and not in the first instance by the courts.⁴⁸

§ 4560. — Presumptions and burden of proof. To warrant a temporary injunction suspending water rates as fixed by a city, substantial evidence that the rate is confiscatory must be furnished.⁴⁹

If the evidence is not conclusive, a practical test is necessary to meet the burden of showing rates confiscatory.⁵⁰

§ 4562. — Scope of review and grounds for attack. What "return a public utility shall be entitled to earn upon its invested capital and what items shall be considered as properly going to make up the sum total of that invested capital are questions of fact for the determination of the commission, and their conclusions thereon, upon which the rate is based, are unassailable unless, as a necessary result, it can be affirmatively asserted that the resultant rate is unreasonable and unlawful." ⁵¹

L. Ed. 908, rev'g, on the ground that no such remedy was provided, 260 Pa. 289, 103 Atl. 744.

⁴⁶ Henry L. Doherty & Co. v. Toledo Railways & Light Co., 254 Fed. 597.

⁴⁷ Port Richmond & Bergen Point Ferry Co. v. Board of Chosen Freeholders of Hudson County, 264 Fed. 998.

⁴⁸ State ex rel. Croy v. Bluefield Waterworks & Improvement Co., — W. Va. —, 103 S. E. 340.

⁴⁹ Water Co. of Tonapah v. Public Service Commission, 250 Fed. 304.

⁵⁰ Kings County Lighting Co. v.

Lewis, 110 N. Y. Misc. 204, 180 N. Y. Supp. 570. See also Lincoln Gas & Elec. Light Co. v. Lincoln, 250 U. S. 256, 63 L. Ed. 968.

The court should not require a trial period of operation under a partial increase in rates which the city was willing to concede, before permitting the full increase asked which appears necessary. City of Toledo v. Toledo Railways & Light Co., 259 Fed. 450.

⁵¹ Per Justice Brooke in City of Detroit v. Michigan Railroad Commission, 209 Mich. 395, 177 N. W. 306.

On "matters involving the exercise of good common sense and judgment only, the determination of the commission must be held to be final unless such determination in its application results in the establishment by 'clear and convincing' proof of a rate so low as to be confiscatory or so high as to be oppressive." ⁵² Order of public service commission fixing rates will not be set aside by the courts merely because a single item of value is regarded as too high or too low.⁵³

§ 4564. — Who may attack. Citizens cannot complain of a raise in street car fares, by authority of the city, where the city had authority to modify the rate contract with the consent of the company.⁵⁴ A city having a rate contract with a public utility may enjoin it from increasing rates as to its citizens although the latter could sue individually or collectively.⁵⁵

§ 4566. Particular methods of review—Injunction suits. In extreme cases, as where a city proposes to compel a street railway company to sell tickets at a clearly confiscatory rate, the court may in advance enjoin such proposed act.⁵⁶ While a court cannot fix rates, it may determine that a lower rate than one proposed would be confiscatory and enjoin such a rate, and where the company seeks to enjoin a rate as unreasonable the court may grant the relief on condition that it will charge no more than what seems to the court to be reasonable.⁵⁷ It is improper, in addition to enjoining enforcement of a rate ordinance, to restrain enforcement of any future ordinances fixing a rate less than that prescribed.⁵⁸

Where a public service commission had no jurisdiction to regulate rates, an injunction suit may join the individual members of the commission as defendants.⁵⁹ In a suit by the mort-

⁵² Per Justice Brooke in *City of Detroit v. Michigan Railroad Commission*, 209 Mich. 395, 177 N. W. 306.

⁵³ *State Public Utilities Commission v. Springfield Gas & Electric Co.*, 291 Ill. 209, 125 N. E. 891.

⁵⁴ *Black v. New Orleans Railway & Light Co.*, 145 La. 180, 82 So. 81.

⁵⁵ *Mobile Elec. Co. v. City of Mobile*, 201 Ala. 607, 79 So. 39.

⁵⁶ *Henry L. Doherty & Co. v. Toledo Railways & Light Co.*, 254 Fed. 597.

⁵⁷ *City of Toledo v. Toledo Railways & Light Co.*, 259 Fed. 450.

⁵⁸ *City of Des Moines v. Des Moines Gas Co.*, 264 Fed. 506.

⁵⁹ *De Pauw University v. Public Service Commission*, 247 Fed. 183.

gagee to enjoin threatened injury to their security by regulation of rates of the corporation, the mortgagor corporation is not a necessary party.⁶⁰

§ 4568. — **Appeals.** Orders of a state commission fixing railroad rates are state laws within the federal statutes allowing direct appeals from the district court to the supreme court in cases where a law of the state is claimed to contravene the Federal Constitution.⁶¹

§ 4572. **Proceedings maintainable by individual consumer or patron.** The city which granted a street franchise to a gas company is entitled to intervene in a suit by consumers to establish a lower rate.⁶²

⁶⁰ De Pauw University v. Public Service Commission, 247 Fed. 183.

⁶¹ Arkadelphia Milling Co. v. St. Louis Southwestern R. Co., 249 U. S. 134, 63 L. Ed. 517.

⁶² Morrell v. Brooklyn Borough Gas Co., 113 N. Y. Misc. 72, 184 N. Y. Supp. 656.

CHAPTER 59

TAXATION

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§ 4659a[New]. In general.

II. OF THE CORPORATION, ITS PROPERTIES, FRANCHISES AND BUSINESS

§ 4577. Power to tax in general. Corporations, like individuals, are not subject to assessment for public improvements, where not benefited thereby.¹

§ 4578. Equality and uniformity—In general. Taxes must be uniform,² and corporate property cannot be assessed for taxation at a higher per cent of its real value than other property.³ However, a gross earnings tax on a certain class of corporations is not required to be an exact equivalent of the ad valorem tax imposed on other corporations.⁴ Whether a cor-

¹ Bush v. Branson, 248 Fed. 377.

² State v. Minnesota Farmers' Mut. Ins. Co., 145 Minn. 231, 176 N. W. 756, applying rule to mutual insurance companies.

³ Union Pac. R. Co. v. Council Bluffs, — Iowa —, 175 N. W. 7.

The valuation of railroad property for taxation must not be excessive as compared with other property. People ex rel. Dale v.

Chicago, L. S. & E. R. Co., 286 Ill. 576, 122 N. E. 109.

An assessment of capital stock is invalid as excessive where greatly in excess of the valuation of other property. People's Gas-light & Coke Co. v. Stuckart, 286 Ill. 164, 121 N. E. 629.

⁴ State v. Wells Fargo & Co., — Minn. —, 179 N. W. 221.

poration whose property has been assessed at its full value, according to a provision requiring full value assessment of all property, is entitled to relief where other property has been intentionally and systematically assessed at less than its full value, is generally answered in the affirmative.⁵

§ 4579. — Classification. For taxation purposes, corporations may be classified according to one of their charter powers although actually engaged in other authorized business.⁶ Classifying different, for purpose of taxation, telegraph and traction companies, is reasonable.⁷ Distilling companies may be made a special class, for the purpose of taxation.⁸ The 1916 Virginia statute imposing a tax on income of domestic corporations derived from sources outside the state denies such corporations the equal protection of the laws, where another statute exempts domestic corporations doing no part of their business within the state from any tax on their income.⁹ In Montana, however, it is held that a state tax based on income may differentiate between corporations according to whether their business is or is not wholly within the state, so far as deduction of taxes and fees of the United States or other country is concerned.¹⁰ The 1917 North Carolina statute requiring payment of a license tax to sell automobiles in the state but reducing the tax four-fifths if the company has three-fourths of its assets invested in the state does not deny to a foreign corporation the equal protection of the laws.¹¹ A statute basing a franchise tax on paid up capital stock of domestic corporations does not arbitrarily discriminate against foreign corporations because the franchise tax on such corporations is based on the amount of capital actually employed within the state.¹² A statute making an addi-

⁵ See note in 3 A. L. R. 1370, annotating *Magnolia Bank v. Board of Supervisors*, 111 Miss. 857, 3 A. L. R. 1365, 72 So. 697.

⁶ *Com. v. John McGlinn Distilling Co.*, 265 Pa. 346, 108 Atl. 823.

⁷ *Postal Telegraph-Cable Co. v. Decatur*, — Ala. App. —, 81 So. 204.

⁸ *Com. v. Hannis Distilling Co.*, 265 Pa. 376, 108 Atl. 822.

⁹ *F. S. Royster Guano Co. v. Com.*, 253 U. S. 412, 64 L. Ed. 989.

¹⁰ *Equitable Life Assur. Soc. Co. v. Hart*, 55 Mont. 76, 173 Pac. 1062.

¹¹ *Bethlehem Motors Corporation v. Flynt*, 178 N. C. 399, 100 S. E. 693.

¹² *Louisville & N. R. Co. v. State*, 201 Ala. 317, 78 So. 93.

tional deduction in assessing bank stock not allowed as to other classes or groups of taxpayers is invalid as violating a constitutional provision requiring a uniform and equal rate of assessment.¹³ The rate per cent of gross earnings tax may be higher in case of express companies than in case of railroad companies.¹⁴

Special statutes often govern the taxation of the property and stock of insurance companies.¹⁵ But insurance companies cannot be classified for taxation on the basis of the salaries which they pay.¹⁶ Stock insurance companies which pay a tax on premiums may be exempted from a statute imposing a tax on intangible personalty of mutual insurance or surety companies, without denying equal protection of the laws.¹⁷

§ 4585. Regulation of interstate or foreign commerce—In general.¹⁸ The right of a foreign corporation to carry on interstate business and to acquire and convey the real property necessary therefor and maintain actions to protect its rights therein is not subject to state taxation.¹⁹ The franchise of a foreign corporation, where exercised exclusively in carrying on interstate commerce, is not subject to taxation by the state; and the fact that the corporation has secured a franchise in the state under which it could, but did not, carry on intrastate business, does not make it taxable.²⁰ A franchise of a foreign corporation to do business in the state is not taxable as property until exercised in some way other than engaging in interstate commerce.²¹ A tax on intrastate business does not interfere with interstate commerce.²²

¹³ *Stillman v. Lynch*, — Utah —, 192 Pac. 272.

¹⁴ *State v. Wells Fargo & Co.*, — Minn. —, 179 N. W. 221.

¹⁵ *Baltimore v. German-American Fire Ins. Co.*, 132 Md. 380, 103 Atl. 980.

¹⁶ *State v. Minnesota Farmers' Mut. Ins. Co.*, 145 Minn. 231, 176 N. W. 756.

¹⁷ *Manufacturers Mut. Fire Ins. Co. v. Clarke*, 41 R. I. 277, 103 Atl. 931.

¹⁸ See also § 5781, *infra*. Special franchise of telegraph com-

pany under federal Post Roads Act not taxable by state, see *People ex rel. Postal Telegraph-Cable Co. v. State Board of Tax Com'rs*, 224 N. Y. 167, 120 N. E. 192.

¹⁹ *People v. Alaska Pac. S. S. Co.*, — Cal. —, 187 Pac. 742.

²⁰ *People v. Alaska Pac. S. S. Co.*, — Cal. —, 187 Pac. 742.

²¹ *People v. Alaska Pac. S. S. Co.*, — Cal. —, 187 Pac. 742.

²² *Postal Telegraph-Cable Co. v. Decatur*, — Ala. App. —, 81 So. 204.

§ 4586. — Property taxes. A state, while it cannot tax the privilege or act of engaging in interstate commerce, may tax the property of the foreign corporation in the state, although chiefly employed in such commerce.²³ For instance, a state may tax property of the Cudahy Packing Company as a freight line company, so far as that property is regularly and habitually used in the state, although chiefly devoted or applied to interstate transportation.²⁴ So railroad property in the state may be taxed although part of a unified system appropriated to interstate commerce.²⁵ Likewise, property of a bridge company, although used in interstate commerce, is taxable.²⁶

§ 4587. — Franchise and license taxes.²⁷ A franchise tax cannot be imposed on a foreign corporation, as a condition of doing business in the state, where its sole business is interstate commerce.²⁸ But a state tax based on the income of a foreign corporation is not a burden on interstate commerce where payment is not made a condition to doing business but instead its enforcement is by the ordinary means of collecting taxes.²⁹ A city may impose an occupation tax on the local business of a corporation engaged in interstate commerce.³⁰ A franchise tax may be imposed on a foreign corporation for the privilege of doing business in the state although it is engaged in interstate commerce.³¹ Where three-fourths of the business of a foreign

²³ Wells, Fargo & Co. v. Nevada, 248 U. S. 165, 63 L. Ed. 190, aff'g State v. Wells, Fargo & Co., 38 Nev. 505, 150 Pac. 836.

Property of a foreign corporation used within the state in interstate commerce is not exempt from taxation, so far as a tax is imposed on capital stock of companies doing business in the state. Com. v. Clyde S. S. Co., — Pa. —, 110 Atl. 532.

²⁴ Cudahy Packing Co. v. Minnesota, 246 U. S. 450, 62 L. Ed. 827, aff'g State v. Cudahy Packing Co., 129 Minn. 30, 151 N. W. 410.

²⁵ State ex rel. Hagerman v. St. Louis & E. St. L. Elec. R. Co., 279 Mo. 616, 216 S. W. 763.

²⁶ People ex rel. McCallister v. Keokuk & Hamilton Bridge Co., 287 Ill. 246, 122 N. E. 467.

²⁷ Franchise tax on foreign corporations as constitutional, see Atlantic Coast Line R. Co. v. State, — Ala. —, 85 So. 424.

²⁸ People ex rel. Pennsylvania Gas Co. v. Saxe, — N. Y. —, 128 N. E. 673, rev'g 186 N. Y. App. Div. 28, 174 N. Y. Supp. 102.

²⁹ Underwood Typewriter Co. v. Chamberlain, 254 U. S. 113, 65 L. Ed. —, aff'g 94 Conn. 47, 108 Atl. 154.

³⁰ Interstate Business Exch. Co. v. Denver, — Colo. —, 190 Pac. 508.

³¹ People ex rel. Pennsylvania

corporation is interstate commerce, a franchise tax must be measured solely by that part of its business which is intrastate commerce.³² The franchise of a foreign corporation exercised in doing interstate commerce is not taxable, although the franchise which it exercises within the state is taxable; and a potential right to carry on intrastate commerce which is not exercised is not taxable.³³ A license tax should not be declared invalid as interfering with interstate commerce, where capable of being applied only to intrastate business.³⁴ A statute imposing an excise tax on capital stock and bonds of foreign corporations does not apply to corporations engaged solely in interstate commerce, where imposed on corporations "previously engaged in business within the state."³⁵ An oil inspection fee, largely exceeding the cost of inspection, cannot be imposed by a state on a foreign corporation so far as the oil is the subject of interstate commerce.³⁶ A Missouri company obtaining orders for ranges through drummers in Louisiana, by showing a sample, and which ships the ranges in carload lots to a salaried agent in Louisiana who causes them to be delivered in the unbroken package to the customers, is engaged in interstate commerce so as not to be subject to a license tax in Louisiana.³⁷

A privilege tax on intrastate business of a telegraph company is within the power of a state.³⁸ A license tax on a telegraph company is not unconstitutional merely because, if sustained, it would require a contribution from interstate commerce busi-

Gas Co. v. Saxe, 186 N. Y. App. Div. 28, 174 N. Y. Supp. 102. See also Bethlehem Motors Co. v. Flynt, 178 N. C. 399, 100 S. E. 693.

A foreign corporation having a place in the state for the transaction of local business entirely separable from its interstate business, may be taxed by the state for the privilege of doing such domestic business. Lawton Spinning Co. v. Com., 232 Mass. 28, 121 N. E. 518; Liquid Carbonic Co. v. Com., 232 Mass. 19, 121 N. E. 514.

³² People ex rel. Pennsylvania Gas Co. v. Saxe, — N. Y. —, 128 N. E. 673, rev'g 186 N. Y. App.

Div. 28, 174 N. Y. Supp. 102.

³³ People v. Alaska Pac. S. S. Co., — Cal. —, 187 Pac. 742.

³⁴ Amos v. Postal Telegraph-Cable Co., 76 Fla. 465, 80 So. 293.

³⁵ Farwell, Ozmun, Kirk & Co. v. Wallace, — N. D. —, 177 N. W. 103.

³⁶ Texas Co. v. Brown, 266 Fed. 577.

³⁷ Ballard v. Wrought Iron Range Co., 144 La. 931, 81 So. 429.

³⁸ Western U. Tel. Co. v. Decatur, 16 Ala. App. 679, 81 So. 199.

ness.³⁹ A license tax which expressly excepts from its operation both government and interstate business cannot be attacked by a telegraph company.⁴⁰

§ 4588. — Basis and mode of valuation. Net incomes of corporations engaged in interstate commerce may be taxed by a state, where dependent on the value of the property in the state.⁴¹ A statute imposing a franchise tax on foreign corporations based on the capital actually employed in the state is not an unwarranted burden on interstate commerce.⁴² The 1913 Minnesota statute imposing a five per cent gross earnings tax on sleeping car companies is not a tax on interstate commerce.⁴³ In taxing a freight line company (Cudahy Packing Company) which furnished cars for a fixed sum per mile which were used in hauling both intrastate and interstate commerce, a tax at a stated per cent of the gross earnings from the mileage within the state, in lieu of other taxes, where not in excess of an ordinary property tax, is a property tax and not a tax on gross earnings so as to burden interstate commerce.⁴⁴ Assessment of tank cars belonging to a foreign corporation and rented by shippers, upon the ratio which miles of railroad in the state over which the cars moved bore to total mileage so traversed in all states, is unreasonable so as to deprive the company of property without due process and also unduly burden interstate commerce.⁴⁵ An excise tax on foreign interstate railroad com-

³⁹ *Postal Telegraph-Cable Co. v. Charlottesville*, — Va. —, 101 S. E. 357.

An occupation tax imposed by a city on a telegraph company does not unlawfully burden interstate commerce merely because the intrastate receipts in the city are insufficient to pay the tax together with other expenses, and hence a portion of the tax must be paid from the receipts on interstate messages. *Fremont v. Postal Telegraph-Cable Co.*, 103 Neb. 476, 172 N. W. 525.

⁴⁰ *Postal Telegraph-Cable Co. v. Decatur*, — Ala. App. —, 81 So. 204.

⁴¹ *Underwood Typewriter Co. v. Chamberlain*, — Conn. —, 108 Atl. 154.

⁴² *Louisville & N. R. Co. v. State*, 201 Ala. 317, 78 So. 93.

⁴³ *State v. Pullman Co.*, — Minn. —, 179 N. W. 224.

⁴⁴ *Cudahy Packing Co. v. Minnesota*, 246 U. S. 450, 62 L. Ed. 827, aff'g *State v. Cudahy Packing Co.*, 129 Minn. 30, 151 N. W. 410.

⁴⁵ *Union Tank Line Co. v. Wright*, 249 U. S. 275, 283, 63 L. Ed. 602, rev'g 146 Ga. 489, 91 S. E. 680, and 143 Ga. 765, 85 S. E. 994, and disapproving dicta to the contrary in *Pullman's Palace*

panies is unconstitutional as an interference with interstate commerce and as a taking of property without due process of law where based on the proportion of mileage in North Dakota to the entire mileage, since that state is one of plains so that cost of construction was less, and because the terminals are in other states.⁴⁶ A state tax measured by the net profits of a corporation, whether a property or a franchise tax, is not invalid merely because most of the profits were derived from interstate commerce.⁴⁷

Where all of certain property of a foreign corporation located in the state is used for both intrastate and interstate commerce, and none of it is used exclusively for either, a franchise tax equal to a certain per cent of the par value of its capital stock employed in business in the state, is not invalid as a tax on interstate commerce nor as violating the due process provision, where the statute provides that corporations are deemed to have employed in the state the proportion of its entire capital stock and surplus that its property and assets in the state bears to all its property and assets wherever located.⁴⁸

§ 4589. Double taxation—Validity. The Fourteenth Amendment does not prohibit double taxation of corporations.⁴⁹

§ 4590. — Existence. In some states, when the property of a corporation has been taxed, its stock is non-taxable.⁵⁰ So it is

Car Co. v. Pennsylvania, 141 U. S. 18, 35 L. Ed. 613.

⁴⁶ *Wallace v. Hines*, 253 U. S. 66, 64 L. Ed. 782.

⁴⁷ *Underwood Typewriter Co. v. Chamberlain*, 254 U. S. 113, 65 L. Ed. —, aff'g 94 Conn. 47, 108 Atl. 154.

⁴⁸ *State ex rel. Wabash Ry. Co. v. Williams*, — Mo. —, 224 S. W. 822, following *St. Louis Southwestern R. Co. v. Arkansas*, 235 U. S. 350, 59 L. Ed. 265.

⁴⁹ *Cream of Wheat Co. v. Grand Forks County*, 253 U. S. 325, 64 L. Ed. 931, aff'g — N. D. —, 170 N. W. 863.

⁵⁰ *Stillman v. Lynch*, — Utah —, 192 Pac. 272.

Where capital stock composed of shares held by another company is taxed, the shares in the hands of the latter cannot be taxed; but the shares are relieved from taxation only to the extent that the capital stock is subjected to taxation, and where a portion of the capital stock of a corporation is not taxed because it represents property permanently located outside the state, shares held by another corporation are to that extent taxable. *Com. v. Shenango Furnace Co.*, — Pa. —, 110 Atl. 721.

Under the 1917 Machinery Act of North Carolina, stock in hands of stockholder as exempt because

the policy of Maryland not to assess both the property and the stock.⁵¹ In Iowa, it is held that where a certain part of the moneyed capital of a bank is actually invested in real estate, and such real estate is fully taxed against the bank as other real estate, the investment cannot be again included in the valuation of the shares for the purpose of taxing the shareholders.⁵² Taxation of capital stock in the domicile is not double taxation because part of the assets representing such capital are taxed in other states.⁵³

A bank is not taxable both on deposits and on capital.⁵⁴ Assessment of a bridge against the owner does not preclude taxation of the corporate grantee of a contract of user of a right of way over the bridge.⁵⁵ Assessment of all the real and personal property of a corporation, where the capital stock has all been invested in such property, does not preclude a back tax upon capital stock.⁵⁶

Payment by a foreign corporation of the general corporation tax for doing business in a state does not exempt it from a tax for inspection of its oils.⁵⁷ A statute requiring foreign corporations which have already paid a fee for entering the state, to pay a privilege tax measured by their capitalization, less the fee already paid, is constitutional.⁵⁸ A franchise tax and a premium or license tax are different and do not amount to double taxation.⁵⁹

§ 4593. Federal agencies and agents—National banks. A state can tax national banks only as to real estate and shares of stock.⁶⁰ Discounts collected but not earned are not taxable

corporation itself pays a tax on capital stock, see *Brown v. Jackson*, 179 N. C. 363, 102 S. E. 739.

⁵¹ *Hyattsville v. Chesapeake & P. Tel. Co.*, 131 Md. 589, 103 Atl. 133.

⁵² *Security Sav. Bank v. Board of Review*, — Iowa —, 178 N. W. 562.

⁵³ *Com. v. Semet-Solvay Co.*, 262 Pa. 234, 105 Atl. 92.

⁵⁴ *Murray v. Board Com'rs Washington County*, 67 Colo. 14, 185 Pac. 262.

⁵⁵ *State ex rel. Hagerman v. St. Louis & E. St. L. Elec. R. Co.*, 279 Mo. 616, 216 S. W. 763.

⁵⁶ *Robertson v. United States Nursery Co.*, 121 Miss. 14, 83 So. 307.

⁵⁷ *Texas Co. v. Brown*, 266 Fed. 577.

⁵⁸ *Mengel Box Co. v. Stevens*, 141 Tenn. 373, 210 S. W. 635.

⁵⁹ *Greene v. National Surety Co.* 186 Ky. 353, 217 S. W. 117.

⁶⁰ *State v. Security Nat. Bank*, 143 Minn. 408, 173 N. W. 885; *Dennis v. First Nat. Bank*, 55

by the state as "profits" of a national bank.⁶¹ Shares of a national bank, held by another national bank, are taxable only to the latter as shareholder, and are not to be included in valuing the shares of the latter when taxing its shareholders; but the interest of a national bank in stock of a state bank can be reached only by a tax upon the shares of the latter and is not taxable to the national bank itself.⁶²

The New York tax against a national bank is based on its capital stock, surplus and undivided profits; and the book value rather than the market value of the stock is the test.⁶³ Items to cover future payment by a national bank of federal income and excess profit taxes are deductible from assessment against the bank under the New York law.⁶⁴

§ 4596. Taxable corporations—Foreign corporations.⁶⁵ A corporation, although a foreign one, is taxable on credits.⁶⁶ A state may tax that portion of a corporation's intangible property which is capital doing business within the state.⁶⁷ A foreign manufacturing corporation does not carry on business or employ capital in New York, so as to be subject to a franchise tax, where it merely maintains one room in New York City with a stenographer in attendance to receive and forward messages and to put customers in touch with the home office.⁶⁸ Stock of another corporation owned by a foreign corporation and held at its general

Mont. 448, 178 Pac. 580; *Stillman v. Lynch*, — Utah —, 192 Pac. 272, quoting *Fletcher Cye. Corp.* § 4593.

⁶¹ *People ex rel. National Park Bank of New York v. Cantor*, 111 N. Y. Misc. 420, 183 N. Y. Supp. 443.

⁶² *Bank of California v. Richardson*, 248 U. S. 476, 63 L. Ed. 372, rev'g 175 Cal. 813, 165 Pac. 152.

⁶³ *People ex rel. National Park Bank of New York v. Cantor*, 111 N. Y. Misc. 420, 183 N. Y. Supp. 443.

⁶⁴ *People ex rel. National Park Bank of New York v. Cantor*, 111

N. Y. Misc. 420, 183 N. Y. Supp. 443.

⁶⁵ Residence for purpose of taxation, see § 395, *supra*.

Meaning of "gross amount of premiums received," in statute relating to taxation of foreign insurance companies, see *State ex rel. Northwestern Mut. Life Ins. Co. v. Tomlinson*, 99 Ohio St. 233, 124 N. E. 220.

⁶⁶ *Singer Sewing Mach. Co. v. Cooper*, 261 Fed. 635.

⁶⁷ *Mexican Petroleum Co. v. Bliss*, — R. I. —, 110 Atl. 867.

⁶⁸ *People ex rel. Brighton Mills v. Knapp*, 192 N. Y. App. Div. 740, 183 N. Y. Supp. 480.

office outside the state is not taxable as assets of the foreign corporation.⁶⁹ A privilege tax of 2 per cent on 47 per cent of the net income of a foreign corporation is not unconstitutional where such a per cent of the income is reasonably attributable to manufacturing carried on by it in the state.⁷⁰ Where a foreign corporation, although engaged in interstate commerce, makes its sales in Illinois where the orders were accepted and where all its property is located, a license tax is properly based on its entire business, rather than its strictly Illinois business, so as to put it on the same footing with domestic corporations.⁷¹ In Virginia, an annual "registration fee," not less than five nor more than twenty-five dollars, is required to be paid by every domestic corporation.⁷²

A state, in taxing foreign corporations, can look beyond its borders only to ascertain the true value of the property within the state, as a part of an organic system of wide extent giving it a value in excess of what it would otherwise possess; and hence the possession of bonds secured by mortgage of lands in other states, or a land grant in another state, cannot be taken into account.⁷³

A tank line company which leases tank cars is not "doing business" in a state where such cars are used by lessees, so as to be subject to taxation.⁷⁴ An Illinois corporation owning and leasing tank cars can be taxed only for the average number in the state during the taxing period.⁷⁵ An oil tank line company, a foreign corporation whose principal place of business is in another state, is taxable as a "car-loaning" company "operating upon railroads in this state," although under a contract executed outside the state.⁷⁶

⁶⁹ *People ex rel. Alpha Portland Cement Co. v. Knapp*, 191 N. Y. App. Div. 262, 181 N. Y. Supp. 32.

⁷⁰ *Underwood Typewriter Co. v. Chamberlain*, — Conn. —, 108 Atl. 154.

⁷¹ *Hump Hairpin Mfg. Co. v. Emmerson*, 293 Ill. 387, 127 N. E. 746.

⁷² See *Elliott's Knob Iron, Steel & Coal Co. v. State Corporation Commission*, 123 Va. 63, 96

S. E. 353, as to forfeiture of charter for failure to pay such fees.

⁷³ *Wallace v. Hines*, 253 U. S. 66, 64 L. Ed. 782.

⁷⁴ *Union Tank Line Co. v. Day*, 143 La. 771, 79 So. 334.

⁷⁵ *Keith Ry. Equipment Co. v. Board of Review*, 283 Ill. 244, 119 N. E. 302.

⁷⁶ *Union Tank Line Co. v. Richardson*, — Cal. —, 191 Pac. 697.

§ 4599. Discriminations against national banks or their shares—Rate of taxation. The federal statutes prohibit the taxation of national bank stock at a greater rate than that assessed on other moneyed capital.⁷⁷

§ 4604. Tangible property of corporation in general.⁷⁸ The Minnesota statute imposing a gross earnings tax of eight per cent on express companies is a valid exercise of the taxing power.⁷⁹ A bank's "declared or nominal capital and surplus," made the basis of an annual license tax, does not include undivided profits.⁸⁰ Under the California statutes, a railroad company is not taxable on gross receipts from a ferry entirely separate from its railroad business.⁸¹

§ 4605. Corporate franchises and privileges.⁸² Franchises are subject to taxation,⁸³ and a "franchise tax" may be an ad

⁷⁷ See *Richmond v. Merchants' Nat. Bank*, 124 Va. 522, 98 S. E. 643.

⁷⁸ Discounted promissory notes of corporation, for current expenses, as taxable as "certificates of indebtedness," see *Com. v. Roxford Knitting Co.*, — Pa. —, 110 Atl. 720.

⁷⁹ *State v. Wells Fargo & Co.*, — Minn. —, 179 N. W. 221.

⁸⁰ *State ex rel. Payne v. Exchange Bank of Natchitoches*, 147 La. 25, 84 So. 481.

⁸¹ *Southern Pac. Co. v. Richardson*, — Cal. —, 184 Pac. 3.

⁸² Franchise tax, what is, see *People ex rel. Pennsylvania Gas Co. v. Saxe*, 186 N. Y. App. Div. 28, 174 N. Y. Supp. 102.

⁸³ *People ex rel. Rochester, S. & E. R. Co. v. Moroney*, 224 N. Y. 114, 120 N. E. 149.

A street franchise is taxable. *State ex rel. Hagerman v. St. Louis & E. St. L. Elec. R. Co.*, 279 Mo. 616, 216 S. W. 763.

Street franchises granted by

the state are taxable. *People ex rel. Postal Telegraph-Cable Co. v. State Board Tax Com'rs*, 224 N. Y. 167, 120 N. E. 192.

A city license to use streets is taxable as "intangible property," it seems. *Central Illinois Public Service Co. v. Swartz*, 284 Ill. 108, 119 N. E. 990.

Franchises of a railroad company subject to taxation include the franchise right to contract and operate a railroad and also a street franchise. *State ex rel. Hagerman v. St. Louis & E. St. L. Elec. R. Co.*, 279 Mo. 616, 216 S. W. 763.

Permission granted by a city to a water company to operate its cable on a bridge is assessable, in connection with its physical property, as a special franchise. *New York & Queens Elec. Light & Power Co. v. Delaney*, — N. Y. —, 128 N. E. 131.

A franchise tax may be imposed by statute on all corporations having express grants from

valorem or property tax.⁸⁴ However, a special franchise cannot exist apart from the ownership of tangible property in the public domain, so far as taxation of such franchises is concerned.⁸⁵ The naked right of eminent domain is not such a franchise as is subject to taxation.⁸⁶ In taxing corporate franchises, good will is to be included, under the California Constitution.⁸⁷ Where a statute imposes an annual franchise tax of a certain per cent on the par value of the capital stock and "surplus," the latter means excess of gross assets above capital stock without deducting debts or liabilities.⁸⁸

A transfer company carrying baggage and passengers is not subject to a franchise tax as a public service company, or a "ferry" company, or as having special or exclusive privileges.⁸⁹ A hotel corporation, because conducting a restaurant in connection with the hotel as a part thereof, is not a "mercantile" corporation, so as to be subject to a franchise tax.⁹⁰

The amount of franchise taxes may be measured by the legislature by any standard it sees fit to adopt; and it is no objection

the legislature to control the waters of great ponds. In re Opinions of Justices, 118 Me. 503, 106 Atl. 865.

Franchise tax, under New York statutes, where railroad company has leased its road, see *People ex rel. Kalbach v. State Tax Commission*, 189 N. Y. App. Div. 347, 178 N. Y. Supp. 486.

Payments made by a power company to a city for permission to lay and operate its conduits and wires on a bridge are "in the nature of a tax," within section 48 of the Tax Law, so as to be deductible from its special franchise tax. *New York & Queens Elec. Light & Power Co. v. Delaney*, — N. Y. —, 128 N. E. 131.

When yearly period begins for license tax on corporate franchises, in New Jersey, see *Old Dominion Copper Mining & Smelt-*

ing Co. v. State Board of Taxes & Assessments, 91 N. J. L. 173, 103 Atl. 79.

⁸⁴ *Greene v. National Surety Co.*, 186 Ky. 353, 217 S. W. 117.

⁸⁵ *People ex rel. Barron v. Knapp*, 183 N. Y. Supp. 750.

What is taxable as "special franchise," see *People ex rel. Barron v. Knapp*, 183 N. Y. Supp. 750.

⁸⁶ *International Smelting Co. v. Tooele County*, — Utah —, 182 Pac. 841.

⁸⁷ *Miller & Lux, Inc. v. Richardson*, — Cal. —, 187 Pac. 411.

⁸⁸ *State ex rel. Marquette Hotel Inv. Co. v. State Tax Commission*, — Mo. —, 221 S. W. 721.

⁸⁹ *Com. v. Louisville Transfer Co.*, 181 Ky. 305, 204 S. W. 92.

⁹⁰ *People ex rel. Beau-Site Co. v. State Board of Tax Com'rs*, 190 N. Y. App. Div. 767, 180 N. Y. Supp. 687.

to a franchise tax that it is measured by the value of the property used in connection with the exercise of it, provided the tax is not merely a property tax under the guise of a franchise tax.⁹¹ The state may fix a franchise tax according to the extent of the use of the franchise or to the extent of the business done.⁹²

§ 4606. Capital stock. A tax on capital stock is a personal property tax.⁹³ "Capital," as distinguished from real estate, of a lumber company, taxable by the state, includes felled timber, railroad ties, manufactured lumber, band sawmills not permanently attached to the land, and machinery not a fixture.⁹⁴ It is held in Mississippi that a domestic corporation is not taxable in that state on the portion of its capital stock invested in shares of the capital stock of another domestic corporation.⁹⁵

In assessing capital stock, the value of the tangible property should be deducted from the fair value of the capital stock, and indebtedness of the corporation should not be deducted but should be considered.⁹⁶ In assessing capital stock, where it has all been invested in property already assessed, the total assessed value of the latter should be deducted from the value of the stock.⁹⁷

§ 4607. Territorial limitations on power to tax.⁹⁸ The place of taxation of corporate property, as regards counties and towns, is often expressly regulated by statute.⁹⁹ A business of a manufacturing company is "carried on," within tax statutes, where the plant is located rather than the county where the office is located.¹

A domestic corporation may be assessed on the amount of

⁹¹ *In re Opinions of Justices*, 118 Me. 503, 106 Atl. 865.

⁹² *State ex rel. Marquette Hotel Inv. Co. v. State Tax Commission*, — Mo. —, 221 S. W. 721.

⁹³ *People ex rel. Little v. St. Louis Merchants' Bridge Co.*, 291 Ill. 95, 125 N. E. 752.

⁹⁴ *Buchanan County v. W. M. Ritter Lumber Co.*, 125 Va. 617, 100 S. E. 546.

⁹⁵ *Robertson v. Mississippi Valley Co.*, 120 Miss. 159, 81 So. 799.

⁹⁶ *Marshalltown Light, Power & Railroad Co. v. Welker*, 185 Iowa 165, 170 N. W. 384.

⁹⁷ *Robertson v. United States Nursery Co.*, 121 Miss. 14, 83 So. 307.

⁹⁸ See also § 395, *supra*.

⁹⁹ *Williams Bros. Mfg. Co. v. Naubuc Fire Dist.*, 92 Conn. 672, 104 Atl. 245.

¹ *Williams Bros. Mfg. Co. v. Naubuc Fire Dist.*, 92 Conn. 672, 104 Atl. 245.

its paid up capital stock, after deducting the value of its property and its debts, although all its tangible property is located outside the state, without violating any constitutional provisions.² In assessing capital stock of a domestic corporation, as distinguished from the property itself, the value of lands owned in another state need not be deducted.³

Capital stock of a foreign corporation can be in the state only in so far as the property of the company, representing it, is in the state.⁴ A state tax on a foreign corporation is not invalid because based on the proportion of the tangible property of the corporation within and without the state, requiring payment of a tax on nearly half the income, where the greater part of the product of the corporation was manufactured in the state, although most of the output was sold in other states.⁵

§ 4609. Taxable situs and place—Realty. The fact that the property and business of a domestic corporation is located in another state does not make it any the less subject to taxation in the state where incorporated.⁶

§ 4610. — Personalty in general. The limitation of the power of a state to tax property which has acquired a permanent situs beyond its boundaries does not apply to personal property outside the state of a corporation's domicile, where it has no permanent situs anywhere.⁷ Under a constitutional provision requiring "all" property to be taxed "in the county where situated," a statute is invalid, so far as in conflict, where it makes personal property of insurance companies taxable at the home office of the owning company.⁸

² Grand Forks County v. Cream of Wheat Co., — N. D. —, 170 N. W. 863.

³ Crossett Lumber Co. v. State, 139 Ark. 357, 214 S. W. 43, following State v. Bodcaw Lumber Co., 128 Ark. 505, 194 S. W. 692.

⁴ Com. v. Clyde S. S. Co., — Pa. —, 110 Atl. 532.

⁵ Underwood Typewriter Co. v. Chamberlain, 254 U. S. 113, 65 L. Ed. —, aff'g 94 Conn. 47, 108 Atl. 154.

⁶ Cream of Wheat Co. v. Grand Forks County, 253 U. S. 325, 64 L. Ed. 931, aff'g — N. D. —, 170 N. W. 863.

⁷ Cream of Wheat Co. v. Grand Forks County, 253 U. S. 325, 64 L. Ed. 931, aff'g — N. D. —, 170 N. W. 863.

⁸ Texas Fidelity & Bonding Co. v. Austin, — Tex. Civ. App. —, 211 S. W. 818; American Indemnity Co. v. Austin, — Tex. Civ. App. —, 211 S. W. 812.

§ 4611. — **Credits.** The situs of intangible personal property of a corporation, for taxation, is the domicile of the corporation; and bank deposits in banks in other states are taxable as are accounts receivable from services and sales outside the state.⁹ Accounts payable to a foreign corporation for business done by a branch in the state, where all the business matters of the branch were attended to at the home office in another state, are not taxable in the state.¹⁰ Money and credits from the local selling stations of the Standard Oil Company have a taxable situs at their locations, as intangible property.¹¹

§ 4612. — **Property in transit.** When an interstate shipment is completed, the property is taxable at the destination.¹²

§ 4613. — **Rolling stock.** Intangible assets and rolling stock of railroad have no situs for taxation, and may be taxed anywhere.¹³ A state may tax movables, such as tank cars, belonging to a foreign corporation, where regularly and habitually used and employed in the state.¹⁴ An oil refinery owning oil cars hauled by a railroad is a "corporation operating rolling stock over any railroad" within the Louisiana statute relating to taxation of rolling stock.¹⁵

§ 4616. **Assessment and valuation.**¹⁶ In taxing corporate property in a state, the intangible value growing out of the

⁹ *Com. v. Semet-Solvay Co.*, 262 Pa. 234, 105 Atl. 92.

Bank deposit outside the state is taxable, in Ohio, against a domestic corporation. *Cleveland & Western Coal Co. v. O'Brien*, 98 Ohio St. 14, 120 N. E. 214.

¹⁰ *National Metal Edge Box Co. v. Readsboro*, — Vt. —, 111 Atl. 386.

¹¹ *Petition of Standard Oil Co. of Indiana*, — Minn. —, 179 N. W. 482.

¹² *Wrought Iron Range Co. v. Rich*, 32 Idaho 453, 184 Pac. 627.

¹³ *State v. Houston & T. C. Ry. Co.*, — Tex. Civ. App. —, 209 S. W. 820.

¹⁴ *Union Tank Line Co. v. Wright*, 249 U. S. 275, 63 L. Ed. 602, rev'g on other grounds, 146 Ga. 489, 91 S. E. 680, and 143 Ga. 765, 85 S. E. 994.

¹⁵ *Constantin Refining Co. v. Day*, 147 La. 623, 85 So. 613.

¹⁶ Method of assessing railroad property for taxation, see generally *Branson v. Bush*, 251 U. S. 182, 63 L. Ed. 215, rev'g 248 Fed. 377.

How franchise valued for taxation, under Kentucky statutes, see *Bosworth v. Kentucky Highlands R. Co.*, 183 Ky. 749, 210 S. W. 671.

company's property situated in another state cannot be considered.¹⁷ Under the Arizona statutes requiring assessment of all taxable property at its full cash value, cash value of the property of a foreign oil company cannot be ignored and its intangible property taxed by capitalizing its earnings or income at twenty-five per cent.¹⁸ Net earnings of a corporation cannot be made the basis of valuation for taxation of property of a gas company, although such earnings may be considered as a fact affecting the true value of the property.¹⁹ In taxing railroad land, special utility of such land for railroad purposes is to be considered in determining value.²⁰ The franchise of a railroad is an element of value, although inseparable, in enhancing the value of its real estate.²¹ In assessing capital stock, the state board of equalization must follow its own rules and cannot take into consideration whether the assessment of the tangible property is high or low.²² A tax for inspection of oil is not a "property" tax within a state constitution providing that all taxation shall be ad valorem.²³ Market value of stock and bonds of a corporation are not conclusive evidence of the value of corporate property, for purposes of taxation.²⁴

A statute providing for a fixed charge on the gross receipts of a freight line company, in lieu of all taxes on the property of the company, used in its business, is a violation of the constitutional rule as to equality and uniformity of taxation and that all property must be assessed at its true value.²⁵

A mistake in the name of the corporation against which property is assessed is not fatal.²⁶

¹⁷ *Franklin v. Nevada-California Power Co.*, 264 Fed. 643.

In fixing the value of the property of a company for taxation, the earnings and income produced by its property in another state is not to be considered. *Standard Oil Co. v. Howe*, 257 Fed. 481.

¹⁸ *Standard Oil Co. v. Howe*, 257 Fed. 481.

¹⁹ *Martineau v. Clear Creek Oil & Gas Co.*, 141 Ark. 596, 217 S. W. 807. But see § 4588, *supra*.

²⁰ *Northern Cent. R. Co. v. Baltimore*, 132 Md. 497, 104 Atl. 44.

²¹ *Missouri Pac. R. Co. v. Conway County Bridge Dist.*, — Ark. —, 218 S. W. 189.

²² *People v. St. Louis Elec. Bridge Co.*, 290 Ill. 307, 125 N. E. 280.

²³ *Texas Co. v. Brown*, 266 Fed. 577.

²⁴ *State v. Wells Fargo & Co.*, — Minn. —, 179 N. W. 221.

²⁵ *Chicago, R. I. & P. R. Co. v. Robertson*, — Miss. —, 84 So. 449.

²⁶ *People ex rel. Troy Union R. Co. v. Mealey*, 224 N. Y. 187, 120 N. E. 155.

In California, although the corporations must make reports to assist in assessing their franchises, the board need not follow such figures but may fix the value according to its discretion.²⁷

§ 4618. Collection of taxes. Penalties for nonpayment of taxes by a corporation are collectible notwithstanding the corporation is in the hands of receivers.²⁸ Equity has jurisdiction of a suit by the United States to impound dividends paid by a corporation now insolvent where such money so paid was fraudulently withheld from the government and should have been paid as taxes.²⁹ Supplementary proceedings against corporations after judgment for a tax are provided for in some states; but a tax on capital invested in a city does not create a personal liability which can be so enforced.³⁰ In Massachusetts, a tax collector cannot levy on shares of stock although he may secure a lien and sell the stock, since the passage of the Uniform Stock Transfer Act.³¹ A personal judgment against stockholders for taxes cannot be obtained in a tax proceeding without personal notice.³²

§ 4619. Remedies for illegal taxation.³³

III. OF THE STOCK, SHAREHOLDERS AND BONDHOLDERS

§ 4620. Taxation of shares—In general.³⁴ A tax on shares of stock is not a tax on property of the corporation, and hence stockholders are not entitled to have a deduction from the value of the shares of the amount of capital stock of the company invested in public building bonds and guaranty fund warrants.³⁵

²⁷ *Miller & Lux, Inc. v. Richardson*, — Cal. —, 187 Pac. 411.

²⁸ *Bright v. Arkansas*, 249 Fed. 953.

²⁹ *United States v. Capital City Dairy Co.*, 252 Fed. 900.

³⁰ *In re Maltbie*, 223 N. Y. 227, 119 N. E. 389.

³¹ *Warr v. Hodges*, — Mass. —, 125 N. E. 557.

³² *State v. Security State Bank*, 143 Minn. 408, 173 N. W. 885.

³³ Statutory procedure to recover back illegal excise tax paid,

see *International Paper Co. v. Com.*, 232 Mass. 7, 121 N. E. 510; *Lever Bros. Co. v. Com.*, 232 Mass. 22, 121 N. E. 516.

³⁴ Tax on stock as tax on corporation or on stockholder, see *State v. Security Nat. Bank*, 143 Minn. 408, 173 N. W. 885.

For article on "Can shares of stock be exempted from taxation in the hands of shareholders?" see 54 Am. L. Rev. 689-704.

³⁵ *Brown v. Hennessey State Bank*, 78 Okla. 141, 189 Pac. 355.

But Liberty Bonds which are exempt from taxation cannot be indirectly taxed by the state, at least in Iowa, by taxing stockholders in banks on the value of their shares based on the capital and earnings, where the bonds are considered in determining the value of the capital.³⁶ In Iowa, by statute, shares of stock are taxable only to the extent of their excess in real value over and above the amount of capital invested in land.³⁷ In determining "surplus profits or reserve funds," within the New York statute as to taxation of corporate stock, corporate assets not taxable in the state are not to be included.³⁸

The state may discriminate between local corporations and individuals by making the former liable to be taxed on shares held in other local corporations, themselves fully taxed, and to be sued for the back taxes, while leaving individuals free from such liabilities.³⁹

A holder of stock is taxable as on a profit, although he does not sell it, where he turns in his stock for stock in a new company to take the place of the old, to the extent of the increase in value of the new stock.⁴⁰

A corporation cannot attack the validity of a tax on its shares in the state where it is created, regardless of the residence of the stockholders, where the statute so providing was in existence at the time of incorporation.⁴¹

The corporation may be required to collect the tax imposed on stock in the hands of stockholders.⁴²

§ 4622. Taxation of corporate bonds. Corporate bonds, where in reality preferred stock are not taxable as bonds.⁴³

§ 4623. Situs of shares of stock in general.⁴⁴ Situs of stock for taxation is not the domicile of the creator of a trust therein

³⁶ *Iowa Loan & Trust Co. v. Fairweather*, 252 Fed. 605, Iowa statute.

³⁷ *Koochiching Co. v. Mitchell*, 186 Iowa 1216, 173 N. W. 151.

³⁸ *People ex rel. Federal Terra Cotta Co. v. Purdy*, 189 N. Y. App. Div. 131, 178 N. Y. Supp. 316.

³⁹ *Ft. Smith Lumber Co. v. Arkansas ex rel. Arbuckle*, 251 U. S. 532, 64 L. Ed. 396, aff'g 138 Ark. 581, 211 S. W. 662; s. c., *State*

ex rel. Attorney General v. Ft. Smith Lumber Co., 131 Ark. 40, 198 S. W. 702.

⁴⁰ *Osgood v. Tax Com'r*, — Mass. —, 126 N. E. 371.

⁴¹ *Koochiching Co. v. Mitchell*, 186 Iowa 1216, 173 N. W. 151.

⁴² See *In re Feliciana Bank & Trust Co.*, 143 La. 46, 78 So. 169.

⁴³ *In re Collier's Estate*, 112 N. Y. Misc. 70, 182 N. Y. Supp. 93.

⁴⁴ Where shares of stock have

but the domicile of the trustees where they had power to sell the stock or handle it as they saw fit.⁴⁵ A membership in the New York stock exchange owned by a resident of Ohio has a taxable situs in that state.⁴⁶

§ 4625. Resident-owned shares in foreign corporations.⁴⁷

§ 4626. **National bank shares.**⁴⁸ A tax on stock, payable by the bank, but in reality a tax against the stockholders, may be imposed by a state on stock of a national bank.⁴⁹ Shares of stock in national banks may be taxed, as against the stockholders, by a state, although the value of the United States obligations are considered in ascertaining the value of the stock.⁵⁰ Where a tax is laid on shares of stock of a national bank in the hands of stockholders, by a state, the value of tax exempt securities of the United States cannot be deducted in assessing the value of the stock.⁵¹

§ 4627a[New]. **Stamp tax on transfers of stock.** In New York, statutes impose a stamp tax on transfers of shares of stock.⁵² A transfer of stock by a corporation as collateral to secure a bond issue is not such a transfer as is subject to the statute.⁵³ Under the New York tax law, a contract to transfer

their situs for purposes of inheritance taxation, under Canada statutes, see *Smith v. Provincial Treasurer of Nova Scotia*, 47 Dom. L. Rep. (Can.) 108.

⁴⁵ *Lowry v. Los Angeles County*, 38 Cal. App. 158, 175 Pac. 702.

⁴⁶ *Anderson v. Durr*, 100 Ohio St. 251, 126 N. E. 57.

⁴⁷ Shares of stock in foreign corporations as taxable against stockholder, under Louisiana statute, see *Ficklen v. City of New Orleans*, 147 La. 567, 85 So. 330.

⁴⁸ Shares of stock of a national bank, extent of power of state to tax, see *Dennis v. First Nat. Bank*, 55 Mont. 448, 178 Pac. 580.

⁴⁹ *State v. Security State Bank*, 143 Minn. 408, 173 N. W. 885.

⁵⁰ *In re First Nat. Bank*, — Neb. —, 171 N. W. 912.

In fixing the value of shares of stock of national banks for taxing purposes, the value due to the bank's ownership of nontaxable stock held by the bank in the Federal Reserve Bank must be included. *First Nat. Bank v. Durr*, 246 Fed. 163.

⁵¹ *In re First Nat. Bank*, — Neb. —, 171 N. W. 912.

⁵² See *Hudson & M. R. Co. v. State*, 227 N. Y. 233, 125 N. E. 202.

What constitutes "transfer of stock" so as to require affixing of stamp, under New York statutes, see *Noble v. Haff*, 172 N. Y. Supp. 139.

⁵³ *Travis v. American Cities Co.*,

stock may be specifically enforced although the contract is not stamped, since the stamp need only be attached when the certificate is delivered.⁵⁴ So a corporation cannot refuse to transfer stock on its books because stamps were not affixed, as required by the New York Tax Law, since the stamps need not be affixed until the transfer is made and the new certificate issued.⁵⁵ Moreover, it is held that stamps on transfer of stock need not be attached at the time of the delivery of the certificate but may be delayed until its indorsement.⁵⁶ Failure to affix stamps renders invalid an assignment of stock executed in another state, where delivered in New York, under the New York statutes.⁵⁷

A stamp tax on the "original" issue of stock does not apply to stock afterwards issued to take the place of other stock.⁵⁸

§ 4628. Assessment and valuation.⁵⁹ In Nebraska, in assessing shares of stock in a bank, real estate mortgage securities, forming part of the bank's assets, should not be excluded.⁶⁰ Stock of a foreign corporation may be taxed although it has no fixed par value.⁶¹

IV. EXEMPTIONS FROM TAXATION

§ 4636. Impairment of contract of exemption.⁶² Whether there is a nonrepealable grant of exemption or merely a repealable privilege is sometimes difficult to determine.⁶³

192 N. Y. App. Div. 16, 182 N. Y. Supp. 394.

⁵⁴ *Lyon v. Farmers' Loan & Trust Co.*, — N. Y. App. Div. —, 184 N. Y. Supp. 380.

⁵⁵ *Smyth v. Pure Ice Co.*, 193 N. Y. App. Div. 479, 184 N. Y. Supp. 305. See also *Lyon v. Farmers' Loan & Trust Co.*, — N. Y. App. Div. —, 184 N. Y. Supp. 380; *Noble v. Haff*, 172 N. Y. Supp. 139. Compare *Luitwieler v. Luitwieler Pumping Engine Co.*, 190 N. Y. App. Div. 80, 179 N. Y. Supp. 463.

⁵⁶ *Reinhard v. Sidney B. Roby Co.*, 110 N. Y. Misc. 152, 179 N. Y. Supp. 781.

⁵⁷ *Luitwieler v. Luitwieler Pumping Engine Co.*, 190 N. Y. App. Div. 80, 179 N. Y. Supp. 463.

⁵⁸ *Edwards v. Wabash Ry. Co.*, 264 Fed. 610.

⁵⁹ Statutory mode of assessing bank stock, see *Security Sav. Bank v. Board of Review*, — Iowa —, 178 N. W. 562; *Pingree Nat. Bank v. Weber County*, — Utah —, 183 Pac. 334; *Continental Nat. Bank v. Naylor*, — Utah —, 179 Pac. 67.

⁶⁰ *Nemaha County Bank v. County Board*, 103 Neb. 53, 170 N. W. 500.

⁶¹ *State ex rel. Standard Tank Car Co. v. Sullivan*, — Mo. —, 221 S. W. 728.

⁶² Legislation as impairing exemption from taxation, see *People ex rel. Troy Union R. Co. v. Mealy*, 224 N. Y. 187, 120 N. E. 155.

⁶³ See *People v. Mealy*, — U. S.

§ 4640. Corporations entitled to exemption.⁶⁴ A corporation organized mainly to bring in new industries to a city, but given power to lend money and invest in stock, bonds, etc., is a "moneyed" corporation within tax exemption statutes of Maryland.⁶⁵

Manufacturing companies are often exempted from taxation.⁶⁶ Under the New York law exempting manufacturing corporations from taxation on capital stock, a company more than half of whose business is the making of clothes is liable to taxes on no more than half of its capital stock.⁶⁷ Stock of a foreign corporation in the hands of resident stockholders, where it has assets within and without the state, is exempt from taxation, where part of the capital is employed in manufacturing in the state, under the Pennsylvania statutes.⁶⁸

The property of educational institutions is often expressly exempted.⁶⁹ Property of an educational institution is not exempt from taxation in Florida so far as it is rented to another or used in part as a residence.⁷⁰

Charitable corporations usually are exempted from taxation.⁷¹ Included in this class of corporations so as to be exempt are a

—, — L. Ed. —, 41 Sup. Ct. 17, holding 1853 statute of New York limiting assessment of a union terminal company to be merely a repealable privilege.

⁶⁴ What constitutes railroad right of way, within exemption from taxation, see *New Castle v. Pittsburgh, Y. & A. Ry. Co.*, 72 Pa. Super. Ct. 135.

Statutory exemption of insane asylums, see *Massachusetts General Hospital v. Belmont*, 233 Mass. 190, 124 N. E. 21; *New England Sanitarium v. Stoneham*, 233 Mass. 171, 124 N. E. 29.

Cemeteries are exempted only where owned by corporations, in *Indiana*. *La Fontaine Lodge v. Eviston*, — Ind. App. —, 123 N. E. 468.

⁶⁵ *Industrial Co. v. State Tax Commission*, 134 Md. 379, 106 Atl. 852.

⁶⁶ *Com. v. Welsh Mountain Mining & Kaolin Mfg. Co.*, 265 Pa. 380, 108 Atl. 722.

⁶⁷ *In re Simecox, Inc.*, 243 Fed. 479.

⁶⁸ *Dupuy v. Johns*, 261 Pa. 40, 104 Atl. 565.

⁶⁹ *Trustees of Thayer Academy v. Board of Assessors*, 232 Mass. 402, 122 N. E. 410.

Property of college exempt, see *Wheaton College v. Norton*, 232 Mass. 141, 122 N. E. 280.

⁷⁰ *Amos v. Jacksonville Realty & Mortgage Co.*, 77 Fla. 403, 81 So. 524.

⁷¹ See *Congregational Sunday School & Publishing Society v. Board of Review*, 290 Ill. 108, 125 N. E. 7; *Davis v. Santa Rosa Infirmary*, — Tex. Civ. App. —, 220 S. W. 125; *Odd Fellows Bldg. Ass'n v. Naylor*, 53 Utah 111, 177 Pac. 214.

Masonic Temple⁷² or a Y. M. C. A.⁷³ But a church publishing house applying all its net proceeds to aiding traveling and worn-out preachers is not a charitable organization so as to be exempt from taxation.⁷⁴

Putting insane asylums in a separate class from other charitable corporations, so far as exemption from taxation is concerned, does not deny them the equal protection of the law.⁷⁵

§ 4641. Property included in exemption—In general.⁷⁶ Exemption of "buildings" of educational corporations includes the land on which they are located and the land adjacent thereto necessary for their proper use, occupancy, and enjoyment, provided the property is not used for private or corporate profit or income.⁷⁷

§ 4642. — Use of property. Exemption of buildings and land "actually used" for charitable purposes does not exempt land where buildings had been destroyed by fire and not replaced.⁷⁸

What are charitable corporations, see generally § 100, *supra*.

The property of a Sunday school and publishing society whose predominant object is to spread the gospel by distribution of its books and Sunday school supplies is exempt from taxation as property of a charitable organization. *Congregational Sunday School & Publishing Society v. Board of Review*, 290 Ill. 108, 125 N. E. 7.

A board aiding the building of churches and supplementing salaries of missionaries is "a purely public charity" so as to be exempt from taxation, except as to income property. *Board of Home Missions & Church Extension of M. E. Church v. City of Philadelphia*, 266 Pa. 405, 109 Atl. 664.

Hospital as a "purely public charity" so as to be exempt from taxation, see *Scott v. All Saints Hospital*, — Tex. Civ. App. —, 203 S. W. 146.

⁷² A lease of part of the building does not affect the exemption.

People ex rel. Syracuse Masonic Temple v. Ostrander, 105 N. Y. Misc. 405, 173 N. Y. Supp. 356.

⁷³ *Corbin Young Men's Christian Ass'n v. Com.*, 181 Ky. 384, 1 A. L. R. 264, 205 S. W. 388.

⁷⁴ *United Brethren Pub. Establishment v. Shaffer*, — Ind. App. —, 123 N. E. 697.

⁷⁵ *Massachusetts General Hospital v. Belmont*, 233 Mass. 190, 124 N. E. 21.

⁷⁶ Extent of exemption of railway property in Canada, see *City of Armstrong v. Canadian Northern Pac. R. Co.*, 48 Dom. L. Rep. (Can.) 268.

Exemption of lodge building of Odd Fellows as used exclusively for charitable, etc., purposes, see *People ex rel. Mizpah Lodge v. Burke*, 228 N. Y. 245, 126 N. E. 703.

⁷⁷ *Mayor, etc., of Gainesville v. Brenau College*, — Ga. —, 103 S. E. 164.

⁷⁸ *Young Women's Christian Ass'n v. Monmouth County Board*

§ 4648. Transfer of exemption.⁷⁹ Tax exemptions, although personal to a railroad company, pass to a lessee.⁸⁰

§ 4649. Effect of consolidation or merger. Merger does not destroy tax exemptions.⁸¹

V. PRIVILEGE TAXES, LICENSES AND INCORPORATION AND STOCK-INCREASE FEES

§ 4651. Privilege taxes and licenses.⁸² A tax for the privilege of doing business is not an income tax, although based on the amount of net income.⁸³ An annual charge for the right to use streets, as imposed by the franchise contract and subject to change, is not a tax or license fee, and an increase from \$100 to \$1,200 a year is proper where not clearly oppressive.⁸⁴ A license fee of one per cent of net income on all corporations engaged in business in the state is within the taxing power.⁸⁵

An occupation tax, where reasonable, may be imposed by a municipality on a telegraph company.⁸⁶ In computing the

of Taxation, 92 N. J. L. 330, 105 Atl. 726.

⁷⁹ Tax upon leasehold interests of lessee in railroad, where leases produced a profit in excess of the rental, held invalid because of lessor's charter exemption from taxation, in *Central of Georgia R. Co. v. Wright*, 248 U. S. 525, 63 L. Ed. 401, rev'g 146 Ga. 406, 91 S. E. 471.

⁸⁰ *Central of Georgia R. Co. v. Wright*, 250 U. S. 519, 63 L. Ed. 1123, rev'g 146 Ga. 406, 91 S. E. 471.

⁸¹ *Central of Georgia R. Co. v. Wright*, 250 U. S. 519, 63 L. Ed. 1123, rev'g 146 Ga. 406, 91 S. E. 471.

⁸² Amount of, see also § 4434, supra.

Occupation taxes, what are, see *Millers' Mut. Fire Ins. Co. v. Austin*, — Tex. Civ. App. —, 210 S. W. 825.

Commutation excise tax on street railways in Massachusetts, see *Harvey v. Bay State St. Ry. Co.*, — Mass. —, 125 N. E. 614.

⁸³ *People ex rel. Barcalo Mfg. Co. v. Knapp*, 187 N. Y. App. Div. 89, 175 N. Y. Supp. 337.

Distinction between excise tax and income tax, see also *Underwood Typewriter Co. v. Chamberlain*, — Conn. —, 108 Atl. 154.

⁸⁴ *Valley Rys. v. Mechanicsburg Borough*, 265 Pa. 222, 108 Atl. 629.

⁸⁵ *Equitable Life Assur. Soc. Co. v. Hart*, 55 Mont. 76, 173 Pac. 1062.

⁸⁶ *Fremont v. Postal Telegraph-Cable Co.*, 103 Neb. 476, 172 N. W. 525.

A pole rental cannot be imposed by a county on a telephone company as a penalty for bad service and high rates, where the county was without power to regulate the service or rates. *Shelby County*

amount of a license fee or occupational tax, against a telegraph company, mileage used solely to transmit interstate messages should not be included.⁸⁷ An annual occupation tax of sixty dollars, imposed on a telegraph company for revenue purposes, on the privilege of doing an intrastate business in a city of over eight thousand people, is not unreasonable although the local business has been conducted at a loss for two years.⁸⁸

§ 4652. Incorporation and stock-increase fees.⁸⁹

VI. INHERITANCE AND SUCCESSION TAXES

§ 4653. Nature and validity of tax in general.⁹⁰ Where stock is delivered by a father to a son, contemporaneously with the execution of his will, and the stock constituted about three-fourths of the estate, the transfer is taxable as one made in contemplation of death, so as to be within the Transfer Inheritance Tax Act, where the donor was 71 years old, notwithstanding the son agreed in return for the stock to pay the donor a life annuity equal in amount to the annual dividend on the stock.⁹¹

§ 4655. Nonresident-owned stock in domestic corporations.⁹² Stock of a domestic manufacturing corporation, owned by a deceased nonresident, is subject to the New York inheritance tax.⁹³ Capital stock of a Minnesota corporation is subject to an inheritance tax in Minnesota although the deceased holder was domiciled in New York, kept his certificates of stock in that state, and the office for the transfer of the stock was in New

v. Cumberland Telephone & Telegraph Co., 140 Tenn. 86, 203 S. W. 342.

⁸⁷ Amos v. Postal Telegraph-Cable Co., 76 Fla. 465, 80 So. 293.

⁸⁸ Fremont v. Postal Telegraph-Cable Co., 103 Neb. 476, 172 N. W. 525.

⁸⁹ See § 225, supra.

⁹⁰ Inheritance tax on transfer of corporate shares, see generally Nickel v. State, 179 Cal. 126, 175 Pac. 641,

Note on "Situs of corporate stock for purposes of succession tax," see Ann. Cas. 1918 A 555.

⁹¹ In re Bottomley's Estate, — N. J. L. —, 111 Atl. 605.

⁹² For note on "Succession tax on bonds of domestic corporation owned by estate of nonresident and held at his residence," see 8 A. L. R. 863, annotating Walker v. People, 64 Colo. 143, 8 A. L. R. 855, 171 Pac. 747.

⁹³ In re Lake's Estate, 112 N. Y. Misc. 681, 183 N. Y. Supp. 335.

York.⁹⁴ Stocks and bonds held by a trustee within the state for a nonresident beneficiary are subject to the direct inheritance tax, where the beneficiary has no control over the property.⁹⁵

§ 4657. Exemption of charitable, religious and educational corporations. The Masonic Lodge is a "charitable" and "benevolent" corporation so as to make devises to it exempt from the transfer tax.⁹⁶

§ 4658. Valuation.⁹⁷ In valuing stock for the purpose of the Transfer Inheritance Tax Act, good will is an asset which may be considered.⁹⁸ An inheritance tax on stock of a domestic railway company is not limited to the proportion of the value of its property in the state to the value of all its property both inside and outside the state.⁹⁹ Shares of stock are presumably worth par, for purposes of the inheritance tax.¹

VII. FEDERAL TAX ON CORPORATION, INCOME AND PROFITS

§ 4659. In general.² The federal income tax cannot be abridged or enlarged by state statutes.³ The only limitation on the power of Congress in the imposition of excise taxes on corporations is that they shall be uniform throughout the United States, i. e., geographically uniform.⁴ Certificates of stock are "property" within the income tax law,⁵ as are bonds.⁶ Net income of a corporation derived from exporting goods and selling them abroad is subject to the 1913 Income Tax Law, and is not unconstitutional as violating the provision "that no tax or duty shall be

⁹⁴ State ex rel. Bodman v: Probate Court, 142 Minn. 415, 172 N. W. 318.

⁹⁵ In re Hostetter's Estate, — Pa. —, 109 Atl. 920.

⁹⁶ In re Hiteman's Estate, 110 N. Y. Misc. 617, 180 N. Y. Supp. 880.

⁹⁷ Valuation of stock for purpose of inheritance tax, see also In re Laidlaw's Estate, 176 N. Y. Supp. 885.

⁹⁸ In re Bottomley's Estate, — N. J. L. —, 111 Atl. 605.

⁹⁹ State ex rel. Bodman v. Pro-

bate Court, 142 Minn. 415, 172 N. W. 318.

¹ Succession of Coleman, — La. —, 85 So. 43.

² Note on "Situs of income of corporation for purpose of income tax," see Ann. Cas. 1918 A 426.

³ Boston & M. R. R. v. United States, 265 Fed. 578.

⁴ Camp Bird v. Howbert, 249 Fed. 27.

⁵ De Ganay v. Lederer, 250 U. S. 376, 63 L. Ed. 1042.

⁶ De Ganay v. Lederer, 250 U. S. 376, 63 L. Ed. 1042.

laid on articles exported from any state.”⁷ Imposition of double liability where the return is false or fraudulent is not unconstitutional as confiscatory.⁸ “False” reports, as used in the 1909 federal income tax relating to corporations means “untrue” and “incorrect” and does not necessarily mean intentionally or fraudulently false.⁹

As to what constitutes income such as to be taxable it is held that rent paid direct to the stockholders instead of to the corporation is part of the income of the corporation;¹⁰ that a building erected by a lessee under a lease prohibiting its removal becomes the property of the lessor when erected and is not taxable as income in a subsequent year in which the lease terminated;¹¹ that amounts received by a water works company for service connections and extensions are “gross income” within the 1909 act, and there cannot be deducted the expense in making the connections and extensions;¹² that where a corporation, pursuant to a scheme of recapitalization, organized another company to which it transferred its property for its stock, except directors’ shares which were of greater par value than the price paid for the property, there was no income, within the Federal Income Tax Law, where the corporation was no richer after the alleged sale than before;¹³ that receipts and accumulations of a business corporation, representing the sale or conversion of its capital, do not constitute taxable income, within the 1909 law.¹⁴ Where property is sold at an advance over the original purchase price, the amount of the advance is a gain or profit for the purpose of computing income.¹⁵ Other items of corporate

⁷ *Peck & Co. v. Lowe*, 247 U. S. 165, 62 L. Ed. 1049, aff’g 234 Fed. 125.

⁸ *Camp Bird v. Howbert*, 249 Fed. 27.

⁹ *United States v. Nashville, C. & St. L. Ry.*, 249 Fed. 678.

¹⁰ *West End St. Ry. Co. v. Malley*, 246 Fed. 625; *Blalock v. Georgia Ry. & Elec. Co.*, 246 Fed. 387; *Rensselaer & S. R. Co. v. Irwin*, 239 Fed. 739.

Where a railway company leased its road on consideration of payment of interest on its bonds direct to the bondholders, and

payment of fixed dividends direct to the stockholders, such payments are income of the lessor, within the 1913 Federal Income Tax. *Rensselaer & S. R. Co. v. Irwin*, 249 Fed. 726.

¹¹ *Cryan v. Wardell*, 263 Fed. 248.

¹² *Union Hollywood Water Co. v. Carter*, 238 Fed. 329.

¹³ *Alpha Portland Cement Co. v. United States*, 261 Fed. 339.

¹⁴ *Biwabik Min. Co. v. United States*, 242 Fed. 9.

¹⁵ *Hays v. Gauley Mountain Coal Co.*, 247 U. S. 189, 62 L. Ed.

income¹⁶ include profits from a sale of stock in another company,¹⁷ dividends received on stock in other companies,¹⁸ etc. On the other hand, corporate dividends which are merely a distribution of capital assets are not taxable as income,¹⁹ nor are stock dividends representing surplus profits transferred to the corporation's capital account.²⁰ However, a dividend of shares

1061, followed in *Scott v. Schwab*, 255 Fed. 57.

¹⁶ Selling price of ore of mining company which was lessee of mine, as income, see *Biwabik Min. Co. v. United States*, 242 Fed. 9.

Where a sole stockholder released a debt owing by him to the corporation, such sum should be treated as capital rather than income of the company, for income tax purposes. *United States v. Oregon-Washington R. & Nav. Co.*, 251 Fed. 211.

¹⁷ The actual value, and not the book value put on stock of another company held by a corporation, must be considered in determining the income in case of sale of such stock. *United States v. Guggenheim Exploration Co.*, 238 Fed. 231.

Profits from stock in a corporation bought by another company before 1909 and sold after Jan. 1, 1909, are income only to the extent that the selling price exceeded the ascertained market value on Jan. 1, 1909. *Cleveland, C., C. & St. L. Ry. Co. v. United States*, 242 Fed. 18.

Where a corporation bought shares of stock of another company before the enactment of the Federal Income Tax Act and sold them afterwards, only the advance deemed to have accrued since Dec. 31, 1908, is corporate income. *United States v. Cleveland, C., C. & St. L. Ry. Co.*, 247 U. S. 195, 62 L. Ed. 1061, aff'g 242 Fed. 18;

Hays v. Gauley Mountain Coal Co., 247 U. S. 189, 62 L. Ed. 1061, rev'g on other grounds 230 Fed. 110.

¹⁸ A dividend on stock of a subsidiary company, paid to the holding company, is income of the latter. *Southern Pac. Co. v. Lowe*, 238 Fed. 847.

An annual dividend received by a corporation is income "accruing" during the year received although earned in part in preceding years. *Skinner v. Union Pac. Coal Co.*, 249 Fed. 152.

Dividends declared in 1910, although paid in part from earnings before 1909, were subject to an excise tax as distinguished from an income tax, in the hands of a corporation as a stockholder. *United States v. Philadelphia, B. & W. R. Co.*, 262 Fed. 188.

¹⁹ *Southern Pac. Co. v. Lowe*, 238 Fed. 847.

Dividends earned by subsidiaries and paid to the parent company, where the earnings were accumulated before the taxing year and had practically become capital, are not subject to income tax, since the transaction should be regarded as bookkeeping rather than as "dividends declared and paid in the ordinary course by a corporation." *Gulf Oil Corporation v. Lewellyn*, 248 U. S. 71, 63 L. Ed. 133, rev'g 245 Fed. 1.

²⁰ *Towne v. Eisner*, 245 U. S. 418, 62 L. Ed. 373, L. R. A. 1918 D 254, rev'g on this question 242 Fed. 702.

owned in another company is not a stock dividend but is subject to the income tax the same as a dividend payable in money.²¹ Accumulations accruing to a corporation through surplus earnings or appreciation in property value, before the 1913 federal act went into effect, are not taxable as income; and this applies to dividends credited to the parent company by a subsidiary whose stock was all owned by the parent company where the dividend merely represented surplus accumulated before 1913.²² The amount of timber bought and afterwards manufactured into lumber and sold, increased in value between the time of purchase and the effective date of the Federal Income Tax Act of 1909, is not income.²³ The increased value of capital is not income,²⁴ and the claim for an income tax cannot be based on mere bookkeeping of a corporation.²⁵ Income tax on insurance corporations, limited to income "received" during the year, includes sums paid agents but not paid over to the treasurer;²⁶ but excess premiums collected and returned to stockholders are not income²⁷ nor are premiums accruing or coming due, but not paid during the tax year.²⁸ Moneys paid by lessees to a mining company as lessor were considered not as converted capital but as rents or royalties so as to be income under the 1909 law.²⁹ Interest on margin accounts, received by a brokerage company, must be listed as part of the gross income, and interest paid by the company on such transactions cannot be deducted in excess of the interest of the debts up to the amount of the capital stock.³⁰

In regard to deductions, and what may be deducted by corporations from their income, under the federal act, it is held that money set apart on the corporate books each year until the

²¹ *Peabody v. Eisner*, 247 U. S. 347, 62 L. Ed. 1152.

²² *Southern Pac. Co. v. Lowe*, 247 U. S. 330, 62 L. Ed. 1142, rev'g 238 Fed. 847.

²³ *Doyle v. Mitchell Bros. Co.*, 247 U. S. 179, 62 L. Ed. 1054, aff'g 235 Fed. 686.

²⁴ *Southern Pac. Co. v. Lowe*, 238 Fed. 847.

²⁵ *Forty Fort Coal Co. v. Kirken-dall*, 233 Fed. 704.

²⁶ *Maryland Casualty Co. v.*

United States, 251 U. S. 342, 64 L. Ed. 297.

²⁷ *New York Life Ins. Co. v. Anderson*, 263 Fed. 527.

²⁸ *Lumber Mut. Fire Ins. Co. v. Malley*, 256 Fed. 380.

²⁹ *Von Baumbach v. Sargent Land Co.*, 242 U. S. 503, 61 L. Ed. 460, rev'g 219 Fed. 31.

³⁰ *Altheimer & Rawlings Inv. Co. v. Allen*, 248 Fed. 688; s. c., 246 Fed. 270.

maturity of certain bonds to meet the loss from selling the bonds below par was not the payment of interest nor did it represent a loss actually sustained within the year, within the Federal Income Tax Law;³¹ that the costs of additions to the equipment or improvements of the road cannot be deducted by a railroad company as "operating expenses" or cost of "maintenance";³² that necessary repairs of ships may be deducted by a corporate shipowner in figuring its tax;³³ that an insurance company the greater part of whose assets is bonds, stocks, etc., may deduct from income the market depreciation of such securities during the year;³⁴ that if there is no paid up capital stock, interest paid on debts not in excess of the paid up capital stock, cannot be deducted;³⁵ and that a corporation receiving dividends from another corporation cannot deduct from its gross income taxes paid on its stock by the latter corporation, if it did not include the amount of such taxes in its return as income.³⁶ The depletion of a mine resulting from the removal of ore in the course of its operation is not a "depreciation of property" for which a deduction may be made under the 1909 law.³⁷ A mining company, for the purpose of determining its net income, is not entitled to deduct from its gross income any amount whatever on account of depletion or exhaustion of ore bodies caused by its operations for the year for which the tax is assessed, nor to deduct the cost value of the ore in the ground before it was mined.³⁸ The corporate lessee of a mine is not entitled to a deduction for depletion in computing its income tax.³⁹ "Paid-up capital stock," as used in the 1909 Federal Excise Tax Act pro-

³¹ *Southern Pac. R. Co. v. Muen-ter*, 260 Fed. 837.

³² *Grand Rapids & I. R. Co. v. Doyle*, 245 Fed. 792, construing 1909 statute.

³³ *San Francisco & P. S. S. Co. v. Scott*, 253 Fed. 854.

³⁴ *New York Life Ins. Co. v. Anderson*, 263 Fed. 527, rev'g 262 Fed. 215.

³⁵ *Associated Pipe Line Co. v. United States*, 258 Fed. 800.

³⁶ *United States v. Aetna Life Ins. Co.*, 260 Fed. 333.

³⁷ *Von Baumbach v. Sargent*

Land Co., 242 U. S. 503, 61 L. Ed. 460, rev'g 219 Fed. 31; *Camp Bird v. Howbert*, 262 Fed. 114.

Value of ore disposed of during tax year held not deductible by lessee of mine as depreciation of capital assets, in *United States v. Biwabik Min. Co.*, 247 U. S. 116, 62 L. Ed. 1017, rev'g 242 Fed. 9.

³⁸ *Goldfield Consol. Mines Co. v. Scott*, 247 U. S. 126, 62 L. Ed. 1022.

³⁹ *Weiss v. Mohawk Min. Co.*, 264 Fed. 502.

viding that interest paid shall be deducted from income "to an amount of such * * * indebtedness not exceeding the paid-up capital stock of such corporation * * * outstanding at the close of the year," means such an amount received by the corporation as does not exceed the par value of the outstanding shares, plus the amount received for any part-paid stock.⁴⁰ It means the paid-up capital stock at par value, and there cannot be added a premium received on sale of its stock, in order to increase the deduction.⁴¹

A corporation,⁴² including railroad⁴³ and street railroad⁴⁴ companies, ceases to do business so as to be not subject to the 1909 statute, where it leases all of its property. Under the 1913 Income Tax Act, however, a corporation is liable to a tax on income although not engaged in business, as where it has leased all its property.⁴⁵ A railroad company which has leased its property for a long term on consideration of payment of interest on bonds direct to bondholders and payment of fixed dividends directly to stockholders, is nevertheless subject to the federal income tax.⁴⁶

A corporation is not "doing business" within the 1909 act, merely because it reduces its indebtedness by means of a sink-

⁴⁰ United States v. New York, N. H. & H. R. Co., 265 Fed. 331, 343, holding that it does not mean "the aggregate amount received by the corporation for the shares, the full-paid stock receipts, and part-paid stock receipts issued by it, even though said sum be in excess of the par value."

⁴¹ Boston & M. R. R. v. United States, 265 Fed. 578.

⁴² New York Mail & Newspaper Transp. Co. v. Anderson, 234 Fed. 590.

What constitutes carrying on business within meaning of 1909 statute, see Von Baumbach v. Sargent Land Co., 242 U. S. 503, 61 L. Ed. 460, rev'g 219 Fed. 31.

⁴³ Old Colony R. Co. v. Gill, 257 Fed. 220.

A railroad company which has

leased all its property to another, paying a fixed rental to the lessor, is not carrying on business within the 1909 law, although it retains its corporate existence, has an office, and makes improvements called for by the lease. Jasper & E. Ry. Co. v. Walker, 238 Fed. 533.

⁴⁴ West End St. R. Co. v. Malley, 246 Fed. 625.

A surrender of its property by a street railroad company for 999 years, in effect a lease, stops the income tax. McCoach v. Continental Passenger R. Co., 233 Fed. 976.

⁴⁵ Rensselaer & S. R. Co. v. Irwin, 249 Fed. 726.

⁴⁶ Northern R. Co. v. Lowe, 250 Fed. 856, following Rensselaer & S. R. Co. v. Irwin, 249 Fed. 726.

ing fund or renews its bonded indebtedness by extending the terms thereof, nor because it disburses money received from the operating company in discharge of corporate obligations.⁴⁷

Where a terminal railway company was organized by four railroad companies, it is subject to the federal excise tax although merely an agency for the four companies.⁴⁸ Where a pipe line company was organized by and did business for only two other pipe line corporations, it was doing business for profit within the Federal Income Tax Law.⁴⁹

The situs of stock and bonds, for the purpose of the federal income tax, may be separated from the domicile of the owner in a foreign country, where held by an agent in this country and the corporations are United States corporations.⁵⁰

Before the 1916 statute, corporate receivers were not subject to the income tax.⁵¹ A fund in the hands of receivers of an insolvent railroad company, representing the net proceeds in operating the road over and above expenses, is not subject to the income tax.⁵² Only net income earned by a trustee while operating the business of a bankrupt corporation is taxable, and hence moneys received by him while not carrying on the business are not taxable.⁵³

So far as stockholders of a corporation are concerned, they are subject to the federal income tax on dividends received by them⁵⁴—except stock dividends⁵⁵—and profits in selling the

⁴⁷ *McCoach v. Continental Passenger R. Co.*, 233 Fed. 976.

⁴⁸ *Houston Belt & Terminal Ry. Co. v. United States*, 250 Fed. 1.

Terminal company whose stock was held by five railroad companies held "organized for profit" and "engaged in business" within Federal Income Tax Act of 1909, in *Boston Terminal Co. v. Gill*, 246 Fed. 664.

⁴⁹ *Associated Pipe Line Co. v. United States*, 258 Fed. 800.

⁵⁰ *De Ganay v. Lederer*, 250 U. S. 376, 63 L. Ed. 1042.

⁵¹ *Scott v. Western Pac. R. Co.*, 246 Fed. 545.

⁵² *Equitable Trust Co. v. Western Pac. Ry. Co.*, 236 Fed. 813.

⁵³ *In re Heller, Hirsh & Co.*, 258 Fed. 208.

⁵⁴ Where dividends are paid during or after 1913, they are taxable as income, in the hands of stockholders, under the surtax provision, although paid from a surplus accumulated before 1913. *Peabody v. Eisner*, 247 U. S. 347, 62 L. Ed. 1152; *Lynch v. Hornby*, 247 U. S. 339, 62 L. Ed. 1149, rev'g 236 Fed. 661.

⁵⁵ *Eisner v. Macomber*, 252 U. S. 189, 64 L. Ed. 521, 9 A. L. R. 1570; *Loomis v. Wattles*, 266 Fed. 876; *United States v. Philadelphia, B. & W. R. Co.*, 262 Fed. 188. *Contra*, *Gulf Oil Corporation v. Lewellyn*, 242 Fed. 709.

stock.⁵⁶ Where the market value of stock had increased to double par value prior to the 1913 Income Tax Act, and afterwards the company sold all its property and distributed the proceeds among its stockholders, the value received in excess of par was not taxable income in their hands, since accruing before 1913.⁵⁷

Stockholders who received the assets of the corporation on its dissolution before the 1916 Federal Income Tax Act increasing the amount of the tax on corporations for that year, are liable for the increase, although the corporation paid before its dissolution the tax payable before the 1916 raise.⁵⁸

A fund loaned to a hospital which is itself exempt from taxation is not subject to the federal income tax where the fund is practically owned by the hospital.⁵⁹

VIII. STATE INCOME TAXES [NEW]

§ 4659a[New]. In general. In several of the states, income taxes are levied on individuals and corporations pursuant to state statutes.⁶⁰ Corporations may be classified separately from

Stock dividends as income for purposes of taxation, see note in 9 A. L. R. 1594.

Stock dividends as taxable, see articles in 20 Columbia L. Rev. 536-549; 33 Harvard L. Rev. 885-901; 18 Michigan L. Rev. 689-692.

⁵⁶ Where a resale of stock is made, interest from the date of the purchase to the date of the sale should not be added to the purchase price to ascertain its cost, in figuring the profit on the sale for income tax purposes. *Hays v. Gauley Mountain Coal Co.*, 247 U. S. 189, 62 L. Ed. 1061, rev'g 230 Fed. 110.

⁵⁷ *Lynch v. Turrish*, 247 U. S. 221, 62 L. Ed. 1087, aff'g 236 Fed. 653.

The amount in excess of the par value and of the actual value of the stock in 1903, derived by a stockholder exclusively from the increase in the value of his stock prior to the date the 1913 act be-

came effective, but first realized by him in cash by a distribution of the proceeds of sale of the corporate property in 1914, is not taxable income. *Lynch v. Hornby*, 236 Fed. 661; *Lynch v. Turrish*, 236 Fed. 653, aff'd 247 U. S. 221, 62 L. Ed. 1087.

⁵⁸ *United States v. McHatton*, 266 Fed. 602.

⁵⁹ *Lederer v. Stockton*, 266 Fed. 676.

⁶⁰ See *Underwood Typewriter Co. v. Chamberlain*, — Conn. —, 108 Atl. 154; *Turkey Knob Coal Co. v. Hallanan*, — W. Va. —, 99 S. E. 849, corporate tax.

A state tax on gross receipts on "business of electric light companies" does not cover receipts of such a company from sale of steam and merchandise. *Com. v. Harrisburg Light & Power Co.*, 262 Pa. 238, 105 Atl. 80.

The 1919 Alabama Income Tax Act was held unconstitutional.

individuals for the purpose of state income taxation.⁶¹ State income tax laws do not surrender the power to tax property of corporations.⁶² A state may impose an income tax on corporations by adopting the definition of net income in the federal income tax statutes.⁶³

A state income tax on corporations may include net income derived from transactions in interstate commerce, figured according to the business done in the state.⁶⁴ A state income tax is not an unlawful burden on interstate commerce because imposed on the net income of a foreign corporation derived from retail sales in the state of milk brought from other states.⁶⁵

The Massachusetts statute imposing an income tax on corporations applies only to such portion of the net income as the United States under its laws actually requires a tax to be paid to it.⁶⁶ A lease of all of a railroad for 99 years precludes taxing the lessor as one "doing business for profit," under the Massachusetts statute.⁶⁷ In that state, dividends, to be taxable as income, need not be paid in money.⁶⁸

Net income, within the New York Income Tax Law, means the same as in the Federal Income Tax Law.⁶⁹ It includes amounts compelled to be paid as excess profits tax.⁷⁰ A foreign corporation cannot complain of the New York Income Tax Law because of being required to adjust its system of accounting and paying

Eliasberg Bros. Mercantile Co. v. Grimes, — Ala. —, 86 So. 56.

⁶¹ State ex rel. Atwood v. Johnson, 170 Wis. 218, 175 N. W. 589.

⁶² Ludlow-Saylor Wire Co. v. Wollbrinck, 275 Mo. 339, 205 S. W. 196.

⁶³ Underwood Typewriter Co. v. Chamberlain, — Conn. —, 108 Atl. 154.

⁶⁴ United States Glue Co. v. Town of Oak Creek, 247 U. S. 321, 62 L. Ed. 1135, aff'g 161 Wis. 211, Ann. Cas. 1918 A 421, 153 N. W. 241.

⁶⁵ Retail sales of milk in Massachusetts by a foreign corporation after being transported from other states is not interstate commerce so as to make net income there-

from exempt from the state income tax. H. P. Hood & Sons v. Com., — Mass. —, 127 N. E. 497.

⁶⁶ American Printing Co. v. Com., 231 Mass. 237, 120 N. E. 686.

⁶⁷ Attorney General v. Ware River R. Co., 233 Mass. 466, 124 N. E. 289; Attorney General v. Boston & A. R. Co., 233 Mass. 460, 124 N. E. 257.

⁶⁸ Wilder v. Trefry, — Mass. —, 125 N. E. 689.

⁶⁹ People ex rel. Barcalo Mfg. Co. v. Knapp, 227 N. Y. 64, 124 N. E. 107, aff'g 187 N. Y. App. Div. 89, 175 N. Y. Supp. 337.

⁷⁰ People ex rel. Barcalo Mfg. Co. v. Knapp, 227 N. Y. 64, 124 N. E. 107, aff'g 187 N. Y. App. Div. 89, 175 N. Y. Supp. 337.

salaries, to the extent required to fulfil the duty of deducting and withholding the tax on income of its officers and employees earned in New York.⁷¹

A Maine corporation doing business in Rhode Island and New York City, and which owns all the stock of a corporation organized by it in New York, cannot deduct the tangible assets of the New York corporation in determining the "corporate excess" under the 1912 Rhode Island statute.⁷²

In Wisconsin,⁷³ the federal income tax cannot be deducted from income in determining the state income tax.⁷⁴ The fact that the surtax of an individual in that state begins with the fourth thousand of income, while that of corporations begins with the first thousand, does not make the income tax invalid.⁷⁵ Under the Wisconsin Income Tax Law of 1917, a dividend paid by a holding company from surplus accrued before 1911 is not taxable as income.⁷⁶

⁷¹ *Travis v. Yale & Towne Mfg. Co.*, 252 U. S. 60, 64 L. Ed. 460, aff'g 262 Fed. 576.

⁷² *Washburn Wire Co. v. Bliss*, — R. I. —, 105 Atl. 179.

⁷³ See *United States Glue Co. v. Town of Oak Creek*, 161 Wis. 211, Ann. Cas. 1918 A 421, 153 N. W. 241.

School corporation held organized for profit so as to be not exempt from state income tax, see *St. John's Military Academy v. Larson*, 168 Wis. 357, 170 N. W. 269.

State income tax on stockholders, under Wisconsin statute, see *State ex rel. Howe v. Lee*, — Wis. —, 178 N. W. 471.

⁷⁴ *State ex rel. Stern Milling Co. v. Wisconsin Tax Com'r*, 170 Wis. 506, 175 N. W. 931.

⁷⁵ *State ex rel. Atwood v. Johnson*, 170 Wis. 218, 175 N. W. 589.

⁷⁶ *State ex rel. Moon v. Nygaard*, 170 Wis. 415, 175 N. W. 810.

CHAPTER 60

COMBINATION, CONSOLIDATION AND MERGER OF CORPORATIONS

I. GENERAL CONSIDERATIONS

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XI. REMEDIES AND PROCEDURE RELATING TO ACTIONS BY OR AGAINST COMPANIES

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XII. CONSOLIDATION OF CORPORATIONS CREATED BY DIFFERENT STATES

§ 4823. Corporation as domestic one in each of states.

§ 4827. Jurisdiction of courts over actions.

I. GENERAL CONSIDERATIONS

§ 4662. What constitutes consolidation—Merger distinguished from consolidation. A consolidation differs from a

merger.¹ Strictly speaking, a consolidation is the unifying of two or more corporations into a single new corporation, while a merger means the absorption of one corporation by another.²

§ 4663. — **Reorganization.** A consolidation or merger is to be distinguished from a reorganization by organization of a new corporation by officers and stockholders of an existing company, with an exchange of stock.³

§ 4665. **Combinations in general distinguished from consolidation and merger—In general.** The American Railway Express Company, formed during the world war, is not a consolidation or merger.⁴

§ 4666. — **Mere purchase and sale of assets.** A mere sale of all the corporate property is to be distinguished from a merger or consolidation.⁵ A purchase of all the corporate assets by another corporation, and the assumption of its debts, does not constitute a merger or consolidation.⁶ Advertising a change as a consolidation and merger does not affect its real nature as a sale.⁷

II. POWER TO CONSOLIDATE OR MERGE

§ 4670. **General rule.** Power to consolidate or merge is not inherent but must be expressly or impliedly conferred.⁸ Corporations not otherwise authorized to consolidate cannot effect a

¹ *State v. Atlantic Coast Line R. Co.*, 202 Ala. 558, 81 So. 60; *Collinsville Nat. Bank v. Esau*, — Okla. —, 176 Pac. 514.

² *State v. Atlantic Coast Line R. Co.*, 202 Ala. 558, 81 So. 60.

³ *Collinsville Nat. Bank v. Esau*, — Okla. —, 176 Pac. 514.

⁴ *McAlister v. American Ry. Exp. Co.*, 179 N. C. 556, 103 S. E. 129.

⁵ *McAlister v. American Ry. Exp. Co.*, 179 N. C. 556, 103 S. E. 129; *Collinsville Nat. Bank v. Esau*, — Okla. —, 176 Pac. 514.

⁶ *Drovers' & Mechanics' Nat. Bank v. First Nat. Bank*, 260 Fed. 9.

A merger is not technically a sale. *Hydraulic Power Co. v. Pettibone Cataract Paper Co.*, 112 N. Y. Misc. 528, 183 N. Y. Supp. 373.

⁷ *Drovers' & Mechanics' Nat. Bank v. First Nat. Bank*. 260 Fed. 9.

⁸ *North American Union v. Johnson*, — Ark. —, 219 S. W. 769.

consolidation by one company purchasing the stock of the other and then dissolving the latter corporation.⁹

§ 4674. Ratification as equivalent to prior grant of power.

A statute ratifying a consolidation agreement does not delegate legislative power to the new company by authorizing it to adopt the name of one constituent and the charter of another constituent.¹⁰ It is not necessary that either the consolidation agreement, or the charter of a constituent with its amendments, be incorporated in statutes ratifying such agreement, and authorizing the new company to adopt as its own the charter of one of the constituent companies.¹¹

§ 4676. Consideration and construction of statutes as permitting or forbidding consolidation—In general.¹²

§ 4677. — Statutes applicable only to particular kinds of corporations. Statutes authorizing consolidation of "street rail-ways" authorizes consolidation of a city line and an interurban line.¹³

§ 4678. Statutory prohibitions—In general. Statutes forbidding consolidation except in case of manufacturing corporations preclude a consolidation of a domestic with a foreign corporation not engaged in manufacturing.¹⁴

§ 4681. — Parallel or competing lines. Statutes prohibiting the consolidation of competing "telegraph" companies have been held applicable to telephone companies created under the statute relating to telegraph companies.¹⁵

⁹In re Doe Run Lead Co., — Mo. —, 223 S. W. 600.

¹⁰Southern R. Co. v. Lancaster, 149 Ga. 434, 100 S. E. 380.

¹¹Southern R. Co. v. Lancaster, 149 Ga. 434, 100 S. E. 380.

¹²Consolidation of cemetery companies as affected by statute, see In re Chauncey, 106 N. Y. Misc. 534, 175 N. Y. Supp. 2.

¹³Milwaukee v. Railroad Commission, 169 Wis. 559, 173 N. W. 329.

¹⁴In re Doe Run Lead Co., — Mo. —, 223 S. W. 600.

¹⁵Cockranton Tel. Co. v. Public Service Commission, 263 Pa. 506, 107 Atl. 23.

§ 4682. Imposing conditions on power to consolidate. Under the Illinois statute authorizing railroad companies incorporated in the state to purchase two-thirds or more of the stock of connecting roads in other states, but providing that the purchaser shall take all the stock that "may be offered" and that the "terms" of purchase of all shares "shall be the same to all stockholders," it is held (1) that the statute applies to a proposition to purchase as well as an "offer"; (2) that the word "terms" includes price; (3) that a stockholder in a connecting road is not bound by his contract to sell at a price less than that paid to other stockholders; (4) that a stockholder who refused to sell his stock is not entitled to hold his stock and then compel its purchase some five years afterwards at the original price offered.¹⁶

§ 4685. Consent of stockholders.¹⁷

III. PROCEDURE TO EFFECT CONSOLIDATION

§ 4691. Contents of the articles or agreement. On consolidation, it may be agreed that one of the constituent companies shall execute an indemnity bond without requiring any such bond from the other constituent companies.¹⁸

§ 4695. Payment of incorporation fees.¹⁹

IV. EFFECT OF CONSOLIDATION OR MERGER AS TO CREATING NEW CORPORATION AND DISSOLVING OLD ONES

§ 4699. General considerations.²⁰ The fact that the property owned by a new corporation is identical with that owned by the old corporation does not preclude the new corporation being a separate and different legal entity.²¹

¹⁶ *Williamson v. Illinois Cent. R. Co.*, — Ind. —, 128 N. E. 758.

¹⁷ Note on "Necessity of assent of all stockholders to consolidation of corporations," see *Ann. Cas.* 1918 A 165.

¹⁸ *Nashville Lumber Co. v. Grayson-McLeod Lumber Co.*, 133 Ark. 599, 202 S. W. 694, construing

such a bond as to liability thereunder.

¹⁹ See § 225, *supra*.

²⁰ Effect of consolidation, see generally *Toledo & C. R. Co. v. Cincinnati, I. & W. R. Co.*, 259 Fed. 813.

²¹ *Osgood v. Tax Commissioner*, — Mass. —, 126 N. E. 371.

§ 4700. Consolidation as creating new company. Rightly understood, there never can be a consolidation of corporations except where the constituent companies cease to exist as separate entities, and a new corporation with the property and assets of the old companies comes into being.²²

§ 4703. Extinguishment of constituent corporations—In general. On consolidation, the constituent companies are deemed dissolved.²³

§ 4706. — Continuance of constituent companies for particular purposes. Consolidation of railroads, under New York statutes, preserves the life of constituent companies for the purpose of meeting obligations of creditors and lienors.²⁴

V. RIGHTS, POWERS, FRANCHISES, PRIVILEGES AND PROPERTY OF CONSOLIDATED OR ABSORBING CORPORATION

§ 4710. As dependent upon nature of combination—In general.²⁵

§ 4711. — Where one corporation merely purchases the property of another. Where a new company is but a continuation of the old, a license to use patent rights passes to the new company.²⁶ A purchase of the assets, name and good-will of a bankrupt corporation passes the right to use the corporate name, including the name of a person as an essential element thereof.²⁷

§ 4712. — In case of consolidation. The powers of a consolidated corporation created under or by virtue of general statutes must be ascertained by referring to such statutes; and under most of the statutes the articles of incorporation may

²² Collinsville Nat. Bank v. Esau, — Okla. —, 176 Pac. 514.

²³ Pennsylvania Utilities Co. v. Public Service Commission, 69 Pa. Super. Ct. 612, and see § 4700, supra.

²⁴ Smith v. Pacific Improvement Co., 104 N. Y. Misc. 481, 172 N. Y. Supp. 65.

²⁵ Effect of merger on powers of

old companies as being powers of new company, see Pennsylvania Utilities Co. v. Public Service Commission, 69 Pa. Super. Ct. 612.

²⁶ Wilson v. J. G. Wilson Co., 241 Fed. 494.

²⁷ G. B. McVay & Son Seed Co. v. McVay Seed & Floral Co., 201 Ala. 644, 79 So. 116.

confer new and additional powers on the consolidated corporation.²⁸ The powers of a consolidated company are generally fixed by statute as including both the powers of the constituent companies and any new powers conferred by the articles of incorporation or the statutes.²⁹

§ 4713. As dependent on laws in force at time of consolidation. Whether the powers and franchises of constituent companies pass to the consolidated company depends on the terms of the consolidation agreement and of the statute under authority of which the consolidation is effected.³⁰

§ 4715. Particular powers and rights acquired. A consolidated public service company, actually doing business, is not required, like a new corporation, to secure a certificate of public convenience.³¹

§ 4720. Power of new or absorbing company to issue stock. On consolidation, where the stock to be issued to stockholders of a constituent company is limited by law to the value of its assets, such stock should be divided among such stockholders in proportion to their holdings, after excluding stock of the old company not issued for value, except where such stock is in the hands of a bona fide purchaser without notice.³² On consolidation, stock of the consolidated company should not be issued share for share of an old company, but only to the extent that the value of the assets of the old company equals the par value of the stock issued.³³

VI. DEBTS, LIABILITIES AND BURDENS

§ 4729. General considerations.³⁴ Specific property of a corporation may be followed by its creditors into a new corpora-

²⁸ Alabama City, G. & A. R. Co. v. Kyle, 202 Ala. 552, 81 So. 54. Public Service Commission, 69 Pa. Super. Ct. 612.

²⁹ Pennsylvania Utilities Co. v. Public Service Commission, 69 Pa. Super. Ct. 612. ³² Taylor v. Citizens' Oil Co., 182 Ky. 350, 206 S. W. 644.

³⁰ Southern R. Co. v. Lancaster, 149 Ga. 434, 100 S. E. 380, and see § 4712, supra. ³³ Taylor v. Citizens' Oil Co., 182 Ky. 350, 206 S. W. 644.

³¹ Pennsylvania Utilities Co. v. ³⁴ Guaranty of accounts of a mercantile corporation as extending to debts of a new corporation

tion where the old company has stripped itself of assets.³⁵ The fact that a renewal note is not signed by the original maker, a corporation, but by its successor, a corporation, which took over its business and assumed its liabilities, does not affect the question whether the renewal note is a payment of the debt.³⁶

§ 4730. Liens and obligations running with the property.³⁷

A judgment which was a lien against a corporation is not necessarily a lien against the property of a company which purchases the assets of the judgment debtor.³⁸ The effect of consolidation on the lien of mortgages of constituent companies is often determined by the terms of the consolidation agreement.³⁹

§ 4741. Special agreement to pay or assume liabilities—In general.⁴⁰

A corporation is liable for the debts or liabilities of its predecessor where it has by express agreement or by reasonable implication assumed their payment.⁴¹ A corporation which is the result of a merger is liable on obligations of the merged corporation where it has expressly assumed such obligations, which assumption may be shown by a resolution of the directors or by the bringing of actions to enforce contracts connected with such obligations.⁴²

§ 4743. — Debts or liabilities included. Assumption of all "obligations of whatsoever character," by a purchasing corporation, includes a liability arising in tort.⁴³ Where one com-

taking over its assets, see *Cooper Grocery Co. v. Eppler*, — Tex. Civ. App. —, 204 S. W. 338.

³⁵ *Collinsville Nat. Bank v. Esau*, — Okla. —, 176 Pac. 514.

³⁶ *Gilland v. Honeywell*, 103 Neb. 50, 170 N. W. 357.

³⁷ Effect of consolidation on mortgage on property of one of the constituent companies, see *Smith v. Pacific Improvement Co.*, 104 N. Y. Misc. 481, 172 N. Y. Supp. 65.

³⁸ *Moore v. Boise Land & Orchard Co.*, 31 Idaho 390, 173 Pac. 117.

³⁹ *Metropolitan Trust Co. v. Chicago & E. I. R. Co.*, 253 Fed. 868.

⁴⁰ Construction of agreement by seller to pay debts out of purchase price, see *Bushong v. R. R. Thompson Estate Co.*, 262 Fed. 297.

⁴¹ *Collinsville Nat. Bank v. Esau*, — Okla. —, 176 Pac. 514.

⁴² *Hydraulic Power Co. v. Pettibone Cataract Paper Co.*, 112 N. Y. Misc. 528, 183 N. Y. Supp. 373.

⁴³ *Geiger v. Sanitary Farm Dairies*, — Minn. —, 178 N. W. 501.

pany purchases the listed assets of another company and assumes its listed liabilities, the former is not liable on a contract of its predecessor to purchase a lot where not included in the lists of assets or liabilities.⁴⁴

§ 4746. Where new corporation created by consolidation—
In general. On merger or consolidation, the new company takes property of the absorbed or a constituent company burdened with any enforceable agreement against the absorbed or constituent company.⁴⁵ Consolidation cannot defeat claims of any creditor of either constituent company.⁴⁶

§ 4747. — Liability for torts. A consolidated corporation is liable for trespasses by a constituent corporation.⁴⁷

§ 4748. — Liability as limited to value of property received.⁴⁸

§ 4750. In case of statutory merger. In case of a merger, the absorbing company is liable for the debts of the absorbed company to the extent of the property and assets received.⁴⁹

§ 4751. In case of mere purchase or transfer of property of another company—General rule. A corporation which purchases the property of another corporation is not liable for the debts of the seller,⁵⁰ in the absence of fraud, especially where all the property is not transferred and the seller continues in business; and this rule applies to the American Railway Express Company formed during the war by agreement between several of the large express companies.⁵¹ But where money is paid

⁴⁴ Little Rock Chamber of Commerce v. Reliable Furniture Co., 138 Ark. 403, 211 S. W. 371.

⁴⁵ Connecticut Co. v. New York, N. H. & H. R. Co., — Conn. —, 107 Atl. 646.

⁴⁶ Johnson v. Barton, — Fla. —, 83 So. 722.

⁴⁷ Sikes v. Moline Consumers' Co., 293 Ill. 112, 127 N. E. 342.

⁴⁸ Sec Okmulgee Window Glass Co. v. Frink, 260 Fed. 159.

⁴⁹ Collinsville Nat. Bank v.

Esau, — Okla. —, 176 Pac. 514, and see § 4746, supra.

⁵⁰ Drovers' & Mechanics' Nat. Bank v. First Nat. Bank, 260 Fed. 9, 15; Warmack v. Major Stave Co., 132 Ark. 173, 200 S. W. 799; Kentucky Distillers' & Warehouse Co. v. Webb's Ex'r, 181 Ky. 90, 203 S. W. 870.

⁵¹ McAllister v. American Ry. Exp. Co., 179 N. C. 556, 103 S. E. 129.

to a corporation not as a corporate entity but on the agreement that it should be immediately distributed among the stockholders, in exchange for their stock, the corporation receives nothing, and hence the purchasing company is liable for the debts of the selling company.⁵²

§ 4757. — Property as subject to equitable lien. It is held in one case that a transfer of all the corporate property passes title free from any equitable lien although the grantee had notice of the claim.⁵³

VII. RIGHTS AND LIABILITIES OF ASSENTING STOCKHOLDERS

§ 4775. Liability for debts of the corporation.⁵⁴

VIII. EFFECT OF UNAUTHORIZED, IRREGULAR OR FRAUDULENT CONSOLIDATION OR COMBINATION

§ 4781. Rights of dissenting stockholders.⁵⁵

IX. DE FACTO CONSOLIDATED CORPORATIONS

§ 4785. General rule.⁵⁶

X. RIGHTS OF DISSENTING STOCKHOLDERS

§ 4791. Injunction against consolidation. The Ohio statute providing that a stockholder who refuses to convert his stock into that of a consolidated company shall be paid the highest market value thereof during the two years preceding the making of the agreement for consolidation, does not provide an adequate remedy for a stockholder who seeks in advance to restrain the corporation from entering into an illegal consolidation, so as to preclude equitable relief.⁵⁷

⁵² Kentucky Distillers' & Warehouse Co. v. Webb's Ex'r, 181 Ky. 90, 203 S. W. 870.

⁵³ C. R. Miller & Bro. v. Mumert, — Tex. Civ. App. —, 196 S. W. 270.

⁵⁴ Consolidation as affecting liability of stockholders of a constit-

uent company, for corporate debts, as dependent on terms of consolidation, 'see American Nat. Bank v. Commercial Nat. Bank, 254 Fed. 249.

⁵⁵ See §§ 4790-4801, *infra*.

⁵⁶ See § 302, *supra*.

⁵⁷ General Inv. Co. v. Lake

§ 4795. Jurisdiction, parties and procedure in actions to prevent or set aside consolidation. In a suit by a stockholder to enjoin a corporation in which he holds stock from entering into an illegal merger with another corporation, such other corporation need not be made a party.⁵⁸ A stockholder may sue to set aside proceedings by which an illegal consolidation was effected, as a cloud upon the corporate title, although neither he nor the corporation is in possession.⁵⁹ The stockholders of a successor company, in an action to which the original company is not a party, cannot attack, merely as stockholders of the successor company, the arrangement by which the original company divested itself of its assets.⁶⁰

XI. REMEDIES AND PROCEDURE RELATING TO ACTIONS BY OR AGAINST COMPANIES

§ 4809. Actions by consolidated or purchasing company. A consolidated company may sue on a guaranty executed by stockholders of the constituent companies for the benefit of the consolidated company.⁶¹

§ 4811. Effect of consolidation or merger while action is pending. Transfer of the assets of plaintiff corporation pending a tort suit does not destroy the cause of action, nor bar relief, in the absence of a proper plea in abatement or the like.⁶² Where a statute provides that a merger shall be without prejudice to the liabilities of the corporations merged, a pending action against the absorbed company is not affected by the merger, and a judgment against the absorbed company may be enforced against the absorbing corporation, and the latter, on paying the judgment, is subrogated to the rights of the absorbed company on a policy of indemnity.⁶³

Shore & M. S. Ry. Co., 250 Fed. 160, 174, aff'g 226 Fed. 976; and see § 4027, supra.

⁵⁸ General Inv. Co. v. Lake Shore & M. S. Ry. Co., 250 Fed. 160, 172, aff'g 226 Fed. 976.

⁵⁹ General Inv. Co. v. Lake Shore & M. S. Ry. Co., 250 Fed. 160.

⁶⁰ Huey v. Patterson, 37 Cal. App. 335, 174 Pac. 939.

⁶¹ Moore v. Baasch, 109 Wash. 568, 187 Pac. 388.

⁶² Wilson & Co. v. Franz, 206 Mich. 581, 173 N. W. 541.

⁶³ Syracuse Lighting Co. v. Maryland Casualty Co., 226 N. Y. 25, 122 N. E. 723, aff'g 178 N. Y. App. Div. 908, 164 N. Y. Supp. 1116.

§ 4813. Evidence of consolidation and presumptions in favor of. Proof of merger of corporations under the New York laws may be made by exemplified copies of public records without producing the original minutes and stock books of the corporation.⁶⁴

XII. CONSOLIDATION OF CORPORATIONS CREATED BY DIFFERENT STATES

§ 4823. Corporation as domestic one in each of states. On consolidation of corporations of different states, a separate corporation is created in each state,⁶⁵ and it is regarded as a domestic corporation in each state.⁶⁶ By absorbing an Alabama railroad company, a Virginia railroad company acquires a local habitat and assumes the legal status of a domestic corporation in Alabama, so far as franchise taxes are concerned.⁶⁷

§ 4827. Jurisdiction of courts over actions. Where a corporation which was a consolidation of corporations of two states sued in one of the states for services, and a counterclaim was interposed for excessive charges paid which was barred in that state, defendant could not enjoin the action in order to compel an action in the other state where the counterclaim was not barred.⁶⁸ Whenever "it is sought to enjoin suit commenced in the state of its creation by a corporation which has lawfully consolidated with the corporation of another state, and the domicile of the corporation bringing the suit is important, its domicile must be held to be in the state of its creation, regardless of the court or the state where the question is raised."⁶⁹

⁶⁴ Barron G. Collier, Inc. v. Kindy, — Minn. —, 178 N. W. 584.

⁶⁵ J. W. Wells Lumber Co. v. Menominee River Boom Co., 203 Mich. 14, 168 N. W. 1011.

⁶⁶ Williamson v. Illinois Cent. R. Co., — Ind. App. —, 121 N. E. 324.

⁶⁷ State v. Atlantic Coast Line R. Co., 202 Ala. 558, 81 So. 60.

⁶⁸ J. W. Wells Lumber Co. v. Menominee River Boom Co., 203 Mich. 14, 168 N. W. 1011.

⁶⁹ J. W. Wells Lumber Co. v. Menominee River Boom Co., 203 Mich. 14, 168 N. W. 1011.

CHAPTER 61

REORGANIZATION

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I. IN GENERAL

§ 4832. Introductory.¹

§ 4834. Definitions and distinctions—Reorganization.²

§ 4836. — Distinguished from combinations, consolidations or mergers.³

¹ Reorganizations generally, see *Brown v. Boston & M. R. R.*, 233 Mass. 502, 124 N. E. 322.

Articles on reorganization, see 20 *Columbia L. Rev.* 733-740.

New schemes of reorganization, see article in 17 *Columbia L. Rev.* 523-537.

² What constitutes a reorganization, see generally *Little Rock*

Chamber of Commerce v. Reliable Furniture Co., 138 Ark. 403, 211 S. W. 371.

Reorganization of bank, what is, see *National Surety Co. v. Sand Springs State Bank*, — Okla. —, 177 Pac. 574.

³ See, on this subject, *Sugg v. Smith*, — Tex. Civ. App. —, 205 S. W. 363, and also § 4663, *supra*.

§ 4841. Power of courts in connection with reorganizations.⁴

Federal courts exercise the right of approval or disapproval of reorganization plans, and where the corporation is in the hands of receivers, resulting in increased profits, and the plan of reorganization was unfair as unduly favoring preferred stockholders, the court properly stays action in regard thereto at a proposed stockholders' meeting.⁵

II. AUTHORITY TO REORGANIZE AND METHODS OF REORGANIZATION

§ 4847. Necessity for, and construction of, statutory authority. Special legislation as to reorganization and consolidation of a particular railroad company and its lessees, where no other railroad company is similarly situated, is constitutional.⁶

§ 4853. Methods of reorganization—Reorganization by voluntary transfer to new company.⁷ A reorganization may be accomplished by the creation of a new corporation by the officers and stockholders of an existing one, who are retained as officers of the new corporation, and an exchange of stock in the new for stock in the old corporation.⁸

§ 4871. Change of state bank into national bank—Effect of reorganization as to rights and liabilities. On reincorporation of a state bank as a national bank, the new bank is liable for usury charged and collected by the old bank.⁹

III. THE REORGANIZATION AGREEMENT

§ 4874. Validity of agreement. There is no illegality in an agreement between bondholders, stockholders, and unsecured creditors of an insolvent mortgagor that there shall be a foreclosure and sale to or for the benefit of a new corporation in which all are to participate.¹⁰

⁴Upset prices in corporate reorganization, see article in 32 Harvard L. Rev. 489-515.

⁵Graselli Chemical Co. v. Aetna Explosives Co., 252 Fed. 456.

⁶Brown v. Boston & M. R. R., 233 Mass. 502, 124 N. E. 322.

⁷By turning over property to new company, see generally Irons

v. Croft Hat & Notion Co., — W. Va. —, 104 S. E. 111.

⁸Collinsville Nat. Bank v. Esau, — Okla. —, 176 Pac. 514.

⁹McCarthy v. Liberty Nat. Bank, — Okla. —, 175 Pac. 940.

¹⁰St. Louis-San Francisco Ry. Co. v. McElvain, 253 Fed. 123, 133.

§ 4883. Construction.¹¹

· § 4888. **Agreement as binding upon new corporation.** Agreement of a committee is binding on the reorganized company where it accepts the benefit of the scheme.¹²

§ 4890. **Specific performance.** Agreement of the committee, impliedly accepted by the reorganized company, to execute notes to creditors of the old company, may be specifically enforced.¹³

VI. WHAT CONSTITUTES JOINDER IN REORGANIZATION AGREEMENT AND EFFECT THEREOF

§ 4907. **Right to rescind.** A bondholder who deposits his bonds with a reorganization committee, pending foreclosure proceedings, cannot withdraw them after decree and sale.¹⁴ A depositing bondholder cannot sue for conversion of his bonds after the plan of reorganization has been finally consummated, regularly and in good faith.¹⁵

VII. COMMITTEE

§ 4912. **General considerations.** A treasurer is not responsible to one turning in stock and bonds for new stock in a reorganized company, for statements in the circular sent to the stockholder by a reorganization committee.¹⁶

§ 4913. **Powers, rights and duties—In general.** A reorganization committee, acting in good faith, may purchase for themselves the corporate property on its dissolution.¹⁷

¹¹ Construction of agreement by creditors to furnish "moneys necessarily required for the operation and conduct of the business," see *Horning v. Louis Peters & Co.*, 202 Mich. 140, 167 N. W. 874.

Corporation held to have taken stock in another company as majority stockholder, and not as underwriter or banker under a reorganization agreement, in *Southern Pac. Co. v. Bogert*, 250 U. S. 483, 63 L. Ed. 1099, modifying 244 Fed. 61.

¹² *McGratty v. Krantz Mfg. Co.*,

183 N. Y. App. Div. 207, 170 N. Y. Supp. 568.

¹³ *McGratty v. Krantz Mfg. Co.*, 183 N. Y. App. Div. 207, 170 N. Y. Supp. 568.

¹⁴ *United States & Mexican Trust Co. v. United States & Mexican Trust Co.*, 250 Fed. 377.

¹⁵ *Carter v. Hughes*, 133 Md. 473, 105 Atl. 583.

¹⁶ *McHugh v. Howlett*, — Mass. —, 125 N. E. 158.

¹⁷ *Anderson v. Johnson*, 277 Mo. 132, 210 S. W. 23.

§ 4919. — **Right to intervene in foreclosure suit.** The mortgage trustee represents all the bondholders and should not permit a committee not representing all the bondholders to select counsel for the trustee to represent it in the foreclosure suit.¹⁸

§ 4921. — **Duty to adopt plan of reorganization before sale in foreclosure suit.** It is "much the better practice for a reorganization committee to formulate their plan for reorganization before the final decree and sale."¹⁹

§ 4924. **Contracts of committee as binding upon bondholders.**²⁰

§ 4926. **Liabilities of committee and their enforcement.** Where the agreement whereby bonds are deposited with a committee gives the committee no power to bind the depositors individually, the committee act as principals and not as agents in dealing with third persons and are personally liable for debts incurred.²¹ The committee may be sued together with the reorganized company for its failure to deliver, as per agreement, notes of the reorganized company given to creditors of the old company.²²

VIII. RIGHTS OF STOCKHOLDERS

§ 4928. **In general.**²³

§ 4933. **Right to participate in reorganization—Rights of nonassenting stockholders where reorganization is not connected with judicial or execution sale.** If a majority stock-

¹⁸ United States & Mexican Trust Co. v. United States & Mexican Trust Co., 250 Fed. 377.

¹⁹ United States & Mexican Trust Co. v. United States & Mexican Trust Co., 250 Fed. 377.

²⁰ Acts of bondholders' committee as committing depositing bondholders to purchase of additional land by new company, see Carter v. Hughes, 133 Md. 473, 105 Atl. 583.

²¹ Mines Management Co. v. Close, 186 N. Y. App. Div. 23, 174 N. Y. Supp. 80.

²² McGratty v. Krantz Mfg. Co., 183 N. Y. App. Div. 207, 170 N. Y. Supp. 568.

²³ Enjoining reorganization, right of stockholder to preliminary injunction, see Demarest v. Winchester Repeating Arms Co., 257 Fed. 162.

holder, by means of a reorganization scheme, prevents minority stockholders from participating, relief should be granted the latter on the theory that the majority stockholder stood in the position of trustee.²⁴ Minority stockholders are not precluded from obtaining relief from a reorganization by a majority stockholder, whereby the latter obtained all the stock of the reorganized corporation, merely because the minority made no contribution towards satisfying the floating indebtedness of the old corporation.²⁵ Minority stockholders should not be given their pro rata share in a new company organized by the majority stockholder without contributing ratably to expenses, etc.²⁶ Minority stockholders, as a condition to compelling the majority stockholder who had reorganized the corporation and taken all the stock, to issue to them their pro rata share of the stock, are properly required to pay their share of the floating indebtedness which had been paid by the majority stockholder.²⁷ A reorganization agreement under which minority stockholders had to pay a much larger assessment per share than the majority stockholder cannot be upheld on the theory that the majority stockholder acted as underwriter or banker, where it was never called upon to pay anything under its guaranty and its purpose was not to act as banker.²⁸

IX. RIGHTS OF BONDHOLDERS

§ 4935. **In general.**²⁹ Bondholders cannot be deprived of their rights by proceeding after reorganization whereby securities are abstracted from the fund created and pledged to secure their debt.³⁰

²⁴ *Southern Pac. Co. v. Bogert*, 250 U. S. 483, 63 L. Ed. 1099, modifying 244 Fed. 61.

²⁵ *Southern Pac. Co. v. Bogert*, 250 U. S. 483, 63 L. Ed. 1099, modifying 244 Fed. 61.

²⁶ *Southern Pac. Co. v. Bogert*, 250 U. S. 483, 63 L. Ed. 1099, modifying 244 Fed. 61.

²⁷ *Southern Pac. Co. v. Bogert*, 250 U. S. 483, 63 L. Ed. 1099, modifying 244 Fed. 61.

²⁸ *Southern Pac. Co. v. Bogert*, 250 U. S. 483, 63 L. Ed. 1099, modifying 244 Fed. 61.

²⁹ Reorganization plan held not a payment of bonds in full. *Lane v. Equitable Trust Co.*, 262 Fed. 918.

³⁰ *Hoyt v. E. I. Du Pont de Nemours Powder Co.*, 88 N. J. Eq. 196, 102 Atl. 666.

X. RIGHTS OF UNSECURED CREDITORS

§ 4948. In general. A reorganization plan for the sale of the property of a bankrupt and a transfer to a company to be formed is invalid as against dissenting creditors.³¹

XI. EFFECT AS CONTINUATION OF CORPORATION OR CREATION OF NEW CORPORATION

§ 4956. Reorganization by voluntary transfer of assets to new company. Whether a conveyance of corporate property from an old to a new company creates a new corporation or merely continues the existence of the original company under a new name, but without any change of identity, depends on the statute under which reorganization was affected, the provisions of the old and new charters, and the proceedings attendant on the reorganization.³² Where a new entity is created by a reorganization, the transfer of the assets to the new company is a "change of title" within the meaning of the forfeiture clause in an insurance policy.³³ A corporation, by transferring all its property to a new company pursuant to a plan of reorganization by which the new company assumes all the liabilities of the old, does not preclude itself from enforcing a contract made by it before the transfer.³⁴

XII. RIGHTS, POWERS AND DUTIES OF NEW COMPANY

§ 4970. Contracts of old company as continuing in favor of new company. Reorganization and a transfer of the corporate assets to a new company does not release the other party to a contract with the old company, where the old company is not dissolved by the reorganization but still continues for winding up purposes.³⁵

³¹ *In re Prudential Outfitting Co.*, 250 Fed. 504.

³² *Bowling v. Continental Ins. Co.*, — W. Va. —, 103 S. E. 285, citing 1 *Fletcher Cyc. Corp.* §§ 4834, 4952, 4953, 4970.

³³ *Bowling v. Continental Ins. Co.*, — W. Va. —, 103 S. E. 285.

³⁴ *Kansas City Soap Co. v. Illinois Cudahy Packing Co.*, 265 Fed. 108.

³⁵ *Illinois Cudahy Packing Co. v. Kansas City Soap Co.*, 247 Fed. 556.

XIII. LIABILITIES OF NEW COMPANY

§ 4981. General rule. The mere fact of reorganization does not render the new company liable on contracts of the old, without regard to the terms of the reorganization.³⁶

§ 4982. Express assumption of debts. Where the reorganized company expressly assumes all the liabilities of the old company, one injured by the old company may sue the new company for the negligence of the old company.³⁷ Usury is no defense where a successor corporation agrees to pay the debts of its predecessor.³⁸

§ 4984. Liability where new company merely a continuation of old company—General rule. A new company substituted for an old company, with a transfer of most of the assets, is liable for the debts of the old company, at least to the extent of the assets received.³⁹ All the property of an old corporation coming into the hands of a new company which is merely a continuation of the old company constitutes a trust fund for the payment of the debts of the old company.⁴⁰ Where a corporation reorganizes under a new name, but with practically the same stockholders and directors, and continues to carry on the same business, equity will regard the new corporation as a continuation of the former corporation, and will hold it liable for the debts of the former corporation.⁴¹ Where a company was reorganized by bondholders

³⁶ *Smith v. Hutchinson Box Board & Paper Co.*, 104 Kan. 732, 180 Pac. 983.

³⁷ *E. I. Du Pont de Nemours & Co. v. Smith*, 252 Fed. 491.

³⁸ *Sugg v. Smith*, — Tex. Civ. App. —, 205 S. W. 363.

³⁹ *Crozier v. Menzies Shoe Co.*, 103 Kan. 565, 175 Pac. 376. To same effect, *Moore v. Boise Land & Orchard Co.*, 31 Idaho 390, 173 Pac. 117, holding, however, in the particular case, the transaction was a sale and not a reorganization; *Skirvin Operating Co. v. Southwestern Elec. Co.*, — Okla. —, 174 Pac. 1069.

Where the management of one corporation organizes another and transfers its property to the new corporation, with the consent of the stockholders, the new corporation is liable for the debts of the other to the extent of the value of the property received. *Hoggan v. Price River Irrigation Co.*, — Utah —, 184 Pac. 536.

⁴⁰ *Okmulgee Window Glass Co. v. Frink*, 260 Fed. 159.

⁴¹ *Stanford Hotel Co. v. M. Schwind Co.*, 180 Cal. 348, 181 Pac. 780.

after foreclosure, and the bondholders were estopped to deny liability on a contract "the result of the performance of which, during a time when their representatives knew that proceedings in their behalf were being taken to foreclose the interest of the mortgagor and to effect a vesting of title in their creature, has been to enhance the value of their property," the reorganized company which assumed the liabilities of the committee is estopped to deny liability.⁴²

Where the new corporation is in its essence but a continuation of the activities and interests of the old company, which retains simply its franchise as a corporation, thus becoming practically extinct as an active entity, creditors of the old company may recover directly against the new company without first obtaining a judgment against the old company.⁴³

Creditors of an old corporation may recover from a new company only to the extent of the assets of the old received by the new company where the new corporation was a distinct entity, created in another state because of the failure of natural gas in the old state, although the property of the old company constituted the basis of capitalization for the new company.⁴⁴

In an action against a company reorganized voluntarily by officers and stockholders merely as a continuation of the old company, for a debt of the old company, the latter is not a necessary defendant.⁴⁵

§ 4985. — Transfer as fraudulent as to creditors of old company.⁴⁶

§ 4986. — Contracts of old company as binding on new company. Where a new company is merely a continuation of an old company, the former is liable on the contracts of the old company.⁴⁷

⁴² Stokes v. Newark Meadows Improvement Co., 90 N. J. Eq. 185, 106 Atl. 132.

⁴³ Okmulgee Window Glass Co. v. Frink, 260 Fed. 159.

⁴⁴ Okmulgee Window Glass Co. v. Frink, 260 Fed. 159.

⁴⁵ Stanford Hotel Co. v. M.

Schwind Co., 180 Cal. 348, 181 Pac. 780.

⁴⁶ Restatement of rule, see Crozier v. Menzies Shoe Co., 103 Kan. 565, 175 Pac. 376.

⁴⁷ Okmulgee Window Glass Co. v. Frink, 260 Fed. 159.

§ 4988. Liability where reorganization in connection with judicial, execution or trustee's sale—General rule. Stockholders of an insolvent corporation, acting in good faith, may purchase the corporate property at a judicial sale, and they take the property free from all contracts of the old company.⁴⁸

§ 4999. Remedy as at law or in equity. Where a new company is merely a continuation of an old company, and the latter merely retains its franchise as a corporation, a suit in equity based on a contract of the old company may be brought against the new company without first suing the old company.⁴⁹ A suit for specific performance of an agreement by the committee to deliver notes to creditors lies against the reorganized company.⁵⁰

⁴⁸ Geo. E. Warren Co. v. A. L. Black Coal Co., — W. Va. —, 102 S. E. 672, citing Fletcher Cyc. Corp. § 4988.

⁵⁰ McGratty v. Krantz Mfg. Co., 183 N. Y. App. Div. 207, 170 N. Y. Supp. 568.

⁴⁹ Okmulgee Window Glass Co. v. Frink, 260 Fed. 159.

CHAPTER 62

INSOLVENCY AND BANKRUPTCY

I. INSOLVENCY

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- § 5132. — Transfers prohibited.
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II. BANKRUPTCY

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I. INSOLVENCY

§ 5008. **What constitutes insolvency; presumptions and proof—Definitions of insolvency and assets; distinctions; statutory definitions.**¹ Capital stock issued and paid for is not a liability, in determining the solvency of a corporation.² A corporation is not insolvent when the value of its property is far greater than the amount of its liabilities, and it is able to pay its debts when they mature, merely because the excess of the value of its property above its liabilities may be much less than the par value of its stock.³

§ 5017. **Assignments for benefit of creditors—Manner of making.** An assignment for benefit of creditors may take the form of a trust deed.⁴ In New York the assignment must comply with the statutes by being acknowledged, recorded, etc.⁵

§ 5020. — **Assignee as trustee; property conveyed.** An assignment of the corporate assets "of every kind" passes all the assets notwithstanding it thereafter particularly mentions specific items.⁶ Whether a corporate mortgage was executed with consent of the stockholders is a question which can be raised by an assignee for benefit of creditors.⁷ The assignee is a "purchaser for value" as against a chattel mortgage not recorded nor

¹ Insolvency, definition, see *Park v. First Nat. Bank*, 23 Ga. App. 167, 97 S. E. 888.

What constitutes insolvency under New Jersey statute, see § 5128, *infra*.

Difference between Delaware and Pennsylvania rule, see *Wheeler v. Badenhausen Co.*, 260 Fed. 991, 995.

² *Fordham v. State*, 148 Ga. 758, 98 S. E. 267.

³ *Shearer v. Farmers' Life Ins. Co.*, 262 Fed. 861.

⁴ *American Surety Co. v. Carbon Timber Co.*, 263 Fed. 295.

⁵ *In re Colwell Lead Co.*, 241 Fed. 922.

⁶ *First Nat. Bank v. Smith*, — W. Va. —, 103 S. E. 318.

⁷ *Leffert v. Jackman*, 227 N. Y. 310, 125 N. E. 446, *aff'g* *Felbel v. Jackman*, 183 N. Y. App. Div. 938, 169 N. Y. Supp. 1093.

possession of the property changed, where he had no knowledge of the mortgage.⁸

§ 5026. — Effect of assignment; dissolution; suits by creditors. After an assignment for benefit of creditors, an officer of the corporation cannot bind the corporation by a new agreement detrimental to the interests of the assignee, and the creditors represented by him.⁹ Where all the corporate assets are assigned to a corporation, and a liquidating committee created, with power to sue to recover assets, a suit in equity to recover assets should be brought by the transferee corporation, it being proper to join the committee and the transferrer corporation.¹⁰

§ 5027. The relation of creditors to insolvent corporations—Trust-fund or American doctrine as to assets of corporations. When a corporation becomes insolvent, its property becomes a trust fund for the benefit of creditors.¹¹ The president and directors of an insolvent corporation are trustees of a trust fund for creditors.¹²

§ 5029. — Nature and extent of doctrine. Even though assets of an insolvent corporation are not deemed a trust fund so as to prevent a preference of creditors, such assets are a trust fund for the payment of debts as distinguished from distribution to officers and stockholders.¹³

§ 5032. — Doctrine as aid to creditors in reaching assets for distribution. The trust-fund theory is enforceable only in equity.¹⁴ Creditors of an insolvent corporation may follow its

⁸ Goodrich v. Woodsome, 78 N. H. 488, 102 Atl. 533.

⁹ Hurley-Mason Co. v. Pacific Commissary Co., — Wash. —, 191 Pac. 624.

¹⁰ First Nat. Bank v. Smith, — W. Va. —, 103 S. E. 318.

¹¹ Weil v. Defenbach, 31 Idaho 258, 170 Pac. 103; Johnson v. United Rys. Co., — Mo. —, 219 S. W. 38; John Miller Co. v. Harvey Mercantile Co., 38 N. D. 531, 165 N. W. 558; Advance-Rumely

Thresher Co. v. Moss, — Tex. Civ. App. —, 213 S. W. 690; P. B. Yates Mach. Co. v. Lakin, — Wash. —, 192 Pac. 982; Williams v. Davidson, 104 Wash. 315, 176 Pac. 334, 181 Pac. 874.

¹² Johnson v. United Rys. Co., — Mo. —, 219 S. W. 38.

¹³ John Miller Co. v. Harvey Mercantile Co., 38 N. D. 531, 165 N. W. 558.

¹⁴ Harris v. Esperanza Min. Co., — N. J. Ch. —, 109 Atl. 826.

assets into the hands of another company so far as the consideration for the transfer of the assets was inadequate.¹⁵

§ 5037. — Right of subsequent creditors to attack a conveyance of corporate property.¹⁶

§ 5038. — Unpaid subscriptions as trust fund.¹⁷ Unpaid stock subscriptions are a trust fund, according to the holdings of the federal courts;¹⁸ but they are not an asset of the company where it was estopped to recover them.¹⁹ In New York, however, the trust-fund doctrine as applied to stock subscriptions is not recognized.²⁰

Where unpaid subscriptions to stock are sold, among other things, at a receiver's sale, the liability of such subscribers is for the full amount of the unpaid balance with the right to share equitably in the actual surplus in the hands of the receiver, and is not limited to the amount necessary, with the amounts due from other corporators, to pay off the corporate indebtedness.²¹

§ 5040. — Present status of trust-fund doctrine; rule governing administration and distribution of assets. The principle of the preference of creditors to stockholders is applicable to all corporations, whether solvent or insolvent, and is wholly independent of the trust-fund theory.²²

§ 5045. Fraudulent conveyances—In general. Fraudulent conveyances by corporations are subject to be set aside by existing creditors the same as if the conveyance was made by an individual.²³ A creditor seeking to establish a trust against

¹⁵ *Johnson v. United Rys. Co.*, — Mo. —, 219 S. W. 38.

¹⁶ See § 5051, *infra*.

¹⁷ See also § 638, *supra*.

¹⁸ *Thoms & Brennenman v. Goodman*, 254 Fed. 39.

¹⁹ *Stoecker v. Goodmāh*, 183 Ky. 330, 209 S. W. 374.

²⁰ *Jeffery v. Selwyn*, 220 N. Y. 77, 6 A. L. R. 1111, 115 N. E. 275.

²¹ *Cosmopolitan Life Ins. Co. v. Sheats*, 20 Ga. App. 622, 93 S. E.

507, holding it no defense that the corporate debts had been discharged by the receiver from the amount derived from such sale.

²² *Adams v. Perryman & Co.*, 202 Ala. 469, 80 So. 853.

²³ *Sanborn-Cutting Co. v. Paine*, 244 Fed. 672. See *Clarke-Woodward Drug Co. v. Hot Lake Sanatorium Co.*, 88 Ore. 284, 169 Pac. 796, holding certain transfers not fraudulent.

the insolvent corporation, because of its fraud, has the burden of proving the fraud, etc.²⁴ A fraudulent conveyance of all the corporate assets to another corporation, without consideration, and a further unauthorized conveyance by the second corporation to the mortgagees of the first corporation, may be set aside by creditors of the first corporation.²⁵ A sale by an insolvent corporation, although made for the express purpose of delaying or defeating a particular creditor, cannot be avoided by such creditor, where made for a good consideration.²⁶

§ 5046. — Transfers of property in good faith. A good faith transfer cannot be attacked as fraudulent where at the time of the transfer the remaining property was amply sufficient to secure creditors, and the creditor stockholder attacking it had recognized the transfer as valid for years and until the corporate business had become unprofitable.²⁷

§ 5047. — Transfers to bona fide purchasers.²⁸

§ 5050. — Right of creditors to follow assets. A creditor may follow corporate property acquired by another corporation with notice through its promoter that the acquisition of the property from the first corporation was in fraud of the creditors of such first company.²⁹ Trust property transferred by the trustee to a subsequently created corporation possessed of other assets may be followed by the beneficiaries into the hands of the corporation.³⁰

A stockholder who receives corporate checks in payment of the treasurer's individual debts, where the treasurer acted without authority, is liable to the corporation or its trustee in bankruptcy for conversion of assets.³¹

²⁴Independent Van & Storage Co. v. Iowa Mercantile Co., — Iowa —, 179 N. W. 157.

²⁵Brayton & Lawbaugh v. Monarch Lumber Co., 87 Ore. 365, 169 Pac. 528, 170 Pac. 717.

²⁶Penny v. Fulljames, 50 Dom. L. Rep. (Can.) 553.

²⁷Singhaus v. Piper, 103 Neb. 493, 172 N. W. 523.

²⁸When fact that purchaser from failing corporation is a bona

fide purchaser for value will protect him, under New Jersey statutes, see Hoover Steel Ball Co. v. Schafer Ball Bearings Co., 89 N. J. Eq. 433, 105 Atl. 500.

²⁹Peabody Consol. Copper Co. v. Maier, 20 Ariz. 370, 181 Pac. 177.

³⁰Hand v. Allen, 294 Ill. 35, 128 N. E. 305.

³¹Heig v. Caspary, 191 N. Y. App. Div. 560, 181 N. Y. Supp. 633.

§ 5051. — Attacks on conveyances or transfers by existing or subsequent creditors. Subsequent creditors cannot attack a prior conveyance by a corporation as fraudulent.³² Thus, a transfer by a corporation of property for shares of its stock is not void as against subsequent creditors where not made for the purpose of defrauding them.³³ In any event, subsequent creditors with knowledge cannot attack a corporate mortgage as fraudulent.³⁴

However, a sale by an insolvent corporation of all its stock and a division of the proceeds among the stockholders is a fraud on existing creditors and also on subsequent creditors who had no notice thereof, where the corporation continued as a going concern but was in fact insolvent.³⁵

§ 5052. Conveyances, transfers, etc., to directors or other officers—In general.³⁶ A fraudulent conveyance by a corporation may take the form of a conveyance by it to a director or other officer.³⁷

§ 5054. — Transfer of assets to other corporations or to a partnership. The fraudulent conveyance which may be set aside by creditors may take the form of the formation of a new company and the conveyance to it of the assets of the old company.³⁸ A transfer of assets by an insolvent corporation to another company having the same officers and practically the same stockholders is void as to existing creditors.³⁹

§ 5055. Withdrawal of assets by stockholders—Rule in general. Stockholders are liable to creditors where assets have been

³² *Scales v. Holje*, — Cal. App. —, 183 Pac. 308.

³³ *Cohen v. George*, 149 Ga. 701, 101 S. E. 803.

³⁴ *Commercial Trust Co. v. L. Wertheim Coal & Coke Co.*, 88 N. J. Eq. 143, 102 Atl. 448.

³⁵ *Johnson v. Canfield-Swigart Co.*, 292 Ill. 101, 126 N. E. 608, aff'g 211 Ill. App. 423.

³⁶ Rights of creditors to attack conveyances of property by a corporation to directors or officers,

see note in 9 A. L. R. 1447, annotating *Beach v. Williamson*, 78 Fla. 611, 9 A. L. R. 1438, 83 So. 860.

³⁷ *John Miller Co. v. Harvey Mercantile Co.*, 38 N. D. 531, 165 N. W. 558.

³⁸ *Schurman v. Improved Plastic-Slate Roofing Co.*, 233 Mass. 499, 124 N. E. 250.

³⁹ *Johnson v. United Rys. Co.*, — Mo. —, 219 S. W. 38.

withdrawn and distributed among them while the corporation was insolvent or where such withdrawal causes insolvency.⁴⁰ But there is no fraudulent conveyance where a corporation distributes bonds and notes to stockholders, where it retains real estate in excess of all debts.⁴¹ If stockholders divide up the assets without paying the debts, creditors may recover from them the proceeds of assets received, and if the stockholders cannot agree among themselves as to the pro rata satisfaction of the decree, any one or more of them may compel contribution pro rata in the usual way.⁴² The power of equity to grant relief to creditors of an insolvent corporation which has fraudulently distributed its property among its stockholders is not limited by the fact that the stockholders cannot be put in statu quo, where the creditors were deceived by their secret and illegal acts.⁴³ Where there is a statute prohibiting the act, fraud of an insolvent corporation, in distributing its property among its stockholders, need not be an actual intent to defraud, in so far as subsequent creditors are concerned.⁴⁴

Where a corporation was insolvent at the time it wrongfully transferred its assets to its stockholders, the amount of recovery in favor of a creditor against a stockholder is limited "to the sum that plaintiff would have received, had the property of the corporation at that time been converted into money and applied to the payment of its debts pro rata," under Stock Corporation Law, § 66.⁴⁵

Alleged invalidity of allotment of bonds received as the purchase price of the corporate property, before dissolution, among

⁴⁰ *Weil v. Defenbach*, 31 Idaho 258, 170 Pac. 103.

Where a sole stockholder appropriates all the corporate assets, so as to make the corporation insolvent, he is personally liable for corporate debts to the extent of such assets. *Fulton Auto Supply Co. v. Sullivan*, 148 Ga. 347, 96 S. E. 875.

A receiver may sue stockholders to compel them to refund sufficient of the corporate funds unlawfully distributed to them, to satisfy a judgment against the corporation.

Weil v. Defenbach, 31 Idaho 258, 170 Pac. 103.

⁴¹ *Saunders v. Hackley & Hume Co.*, 275 Mo. 41, 204 S. W. 269.

⁴² *Adams v. Perryman & Co.*, 202 Ala. 469, 80 So. 853.

⁴³ *Johnson v. Canfield-Swigart Co.*, 292 Ill. 101, 126 N. E. 608, *aff'g* 211 Ill. App. 423.

⁴⁴ *Johnson v. Canfield-Swigart Co.*, 292 Ill. 101, 126 N. E. 608, *aff'g* 211 Ill. App. 423.

⁴⁵ *Kelly v. Mendelson*, 176 N. Y. Supp. 464.

the stockholders, as violating a statute forbidding division or withdrawal of the capital stock, cannot be urged where no creditor objects and all the stockholders have agreed to it.⁴⁶

§ 5056. — Payment of dividends. Where the corporation is insolvent, dividends paid to stockholders in violation of a statute are recoverable in behalf of the corporation.⁴⁷

§ 5057. — Purchase of stock by corporation.⁴⁸ A purchase of its own stock when insolvent is voidable as to existing creditors, and if notes or bonds are given in exchange for such stock they will be subordinate to the claims of existing creditors; and the same is true as to subsequent creditors who become such without notice of the purchase.⁴⁹ Where one stockholder sells his stock to another, and receives his pay not from the buyer but from the assets of the corporation, he is liable, to the extent of the value of the assets received, to creditors.⁵⁰ A stockholder who disposes of his stock with knowledge that the money received in payment thereof is taken from corporate funds, resulting in a depletion of the capital stock of the company, and with the further knowledge that the company is to continue business, is accountable, where the company afterwards becomes insolvent, for the money received, to subsequent creditors without notice.⁵¹

§ 5058. — Unpaid subscription; release of liability.⁵²

§ 5062. Recovery of assets wrongfully transferred; setting aside fraudulent conveyances—Limitation of actions; estoppel. Laches may preclude the right of a creditor stockholder to attack a transfer as fraudulent.⁵³ Limitations do not begin to run against a cause of action against stockholders because of distribution of corporate assets among stockholders while debts

⁴⁶ Chadwick v. Holm, 31 Idaho 252, 170 Pac. 87.

⁴⁷ Hyde v. Scott, 47 Dom. L. Rep. (Can.) 260.

⁴⁸ See also § 1141, supra.

⁴⁹ First Trust Co. v. Illinois Cent. R. Co., 256 Fed. 830.

⁵⁰ Garrow v. Fraser, 98 Wash. 88, 167 Pac. 75.

⁵¹ Johnson v. Canfield-Swigart Co., 211 Ill. App. 423, 429, aff'd 292 Ill. 101, 126 N. E. 608.

⁵² See § 639, supra.

⁵³ Singhaus v. Piper, 103 Neb. 493, 172 N. W. 523.

existed, as against a judgment creditor, until he has notice that the assets of the corporation are not sufficient to satisfy his debt.⁵⁴

§ 5066. Distribution of assets of insolvent corporations; preferences in general—Equality of distribution.⁵⁵ Assets of an insolvent corporation are applied first to secured debts and then to unsecured debts pro rata.⁵⁶ One who sells his stock to his corporation cannot share with ordinary creditors in bankruptcy proceedings.⁵⁷ A claim for money paid a bank to pay up a note, where the bank fraudulently concealed the transfer of the note to another bank, is entitled to priority, where the bank becomes insolvent.⁵⁸

Unless otherwise provided by statute, a claim for moneys received as guardian, is not entitled to priority, in case of an insolvent trust company, where all money received has been commingled and placed in a common fund.⁵⁹

When a corporation is liquidated, those entitled to the income of the trust are to be awarded so much of the sums received for the stock as they show was income accruing after their right to income began, and the balance goes to the principal.⁶⁰

§ 5070. — Creditors with collateral or additional promises; marshalling assets.⁶¹ A mortgage creditor of an insolvent corporation may prove his claim for the full amount without crediting a collection in part by a foreclosure of the mortgage.⁶²

§ 5071. — Preferences to debts of receivers; rent. The cost of repairs which the tenant should have made but which the land-

⁵⁴ Weil v. Defenbach, 31 Idaho 258, 170 Pac. 103.

⁵⁵ Judgment in proceeding for distribution of assets of insolvent corporation, as res judicata, see Perkins v. Le Viness, 134 Md. 252, 106 Atl. 705.

Effect of Bankruptcy Act, see Smith v. Powers, 255 Fed. 582.

⁵⁶ Clarke-Woodward Drug Co. v. Hot Lake Sanatorium Co., 88 Ore. 284, 169 Pac. 796.

⁵⁷ Keith v. Kilmer, 261 Fed. 733, 9 A. L. R. 1287.

⁵⁸ State ex rel. Crittenberger v. Farmers' & Merchants' Bank, — Ind. App. —, 124 N. E. 501.

⁵⁹ Wainwright Trust Co. v. Dublin, — Ind. App. —, 119 N. E. 387.

⁶⁰ In re McKeown's Estate, 263 Pa. 78, 106 Atl. 189.

⁶¹ Rule in bankruptcy proceedings, see In re Battle Island Paper Co., 259 Fed. 921.

⁶² Goodman Mfg. Co. v. Pittsburgh-Buffalo Co., 265 Fed. 561.

lord made, even if called rent, is not rent entitled to priority in administering the estate of an insolvent corporation.⁶³ Interest which a tenant agreed to pay on the balance of the cost of a building to be erected (where a certain per cent of the cost was to be paid by the tenant), under an agreement to purchase the building, is not rent so as to be entitled to priority.⁶⁴

§ 5072. — Preference to states or to the United States.⁶⁵ State taxes are entitled to a preference in insolvency proceedings.⁶⁶

§ 5073. Claims for labor, wages and material. Claims for wages are often given priority by statute, in case of insolvent corporations.⁶⁷ Taking notes for wages does not waive the priority of a laborers' lien.⁶⁸

§ 5074. Right of corporation to prefer creditors—General rule permitting preferences; effect of trust-fund doctrine. In North Dakota an insolvent corporation may prefer creditors.⁶⁹ In Oklahoma, an insolvent corporation may prefer creditors the same as an individual, and hence it may make a mortgage to secure a loan.⁷⁰ A statute giving "a debtor" the right to prefer creditors applies to corporations.⁷¹

The right of a corporation to prefer creditors cannot be transferred to another corporation having the same officers so as to authorize the latter to administer the assets.⁷²

⁶³ *In re Receivership of Lightwell Steel Sash Co.*, — Del. —, 105 Atl. 376.

⁶⁴ *In re Receivership of Lightwell Steel Sash Co.*, — Del. —, 105 Atl. 376.

⁶⁵ State as preferred creditor, in suit to wind up insolvent bank, see *American Surety Co. v. Pearson*, — Minn. —, 178 N. W. 817, construing Minnesota bank statutes.

⁶⁶ *Winsor v. Pilgrim Shoe Machinery Co.*, — R. I. —, 105 Atl. 397.

⁶⁷ *Steel & Iron Mongers v. Bonnite Insulator Co.*, 90 N. J. Eq.

200, 106 Atl. 380, and see § 5394, *infra*.

⁶⁸ *Armstrong v. Watson*, 45 Dom. L. Rep. (Can.) 501.

⁶⁹ *John Miller Co. v. Harvey Mercantile Co.*, 38 N. D. 531, 165 N. W. 558.

⁷⁰ *Union Trust Co. v. Hendrickson*, — Okla. —, 172 Pac. 440.

⁷¹ *Merced Bank v. Ivett*, 127 Cal. 134, 59 Pac. 393; *John Miller Co. v. Harvey Mercantile Co.*, 38 N. D. 531, 165 N. W. 558.

⁷² *Johnson v. United Rys. Co.*, — Mo. —, 219 S. W. 38.

The right of a corporation to prefer creditors cannot, by agreement between it and them, be extended to a time when, because of insolvency, it has been restrained from disposing of property or transacting business.⁷³

§ 5075. — Rule denying right to prefer creditors; trust-fund doctrine as prohibition. In Washington, an insolvent corporation “will not be permitted to do or suffer anything which will permit one or more creditors to obtain a preference, no matter what the good faith of such creditor may be.”⁷⁴

An unlawful preference by a debtor corporation is a fraud on other creditors.⁷⁵

§ 5080. — Preferences in pursuance of prior agreements. Preferences agreed upon when the corporation was solvent are not invalid because of the insolvency of the corporation when the preference was consummated.⁷⁶

§ 5082. — Advances by creditors.⁷⁷

§ 5085. — Notice to creditors of insolvency. Payments made to creditors when a corporation is insolvent, with knowledge of the insolvency, are voidable and may be recovered by the receiver.⁷⁸ However, a creditor of a corporation “is not, as a matter of law, chargeable with notice of the insolvency of the corporation with which he deals”;⁷⁹ but knowledge of insolvency may be imputed by knowledge of facts which would put a prudent man on inquiry.⁸⁰ A creditor may be chargeable with notice of insolvency of a corporation at the time it made payments

⁷³ Corporate officers cannot agree with an agent to allow him to collect money on account of the corporation and appropriate it in payment of his individual claim, after the insolvency of the company and while it is enjoined from transacting any business or disposing of its assets. *O’Neil v. Burnett*, 263 Pa. 216, 106 Atl. 246.

⁷⁴ *Williams v. Davidson*, 104 Wash. 315, 176 Pac. 334, 181 Pac. 874.

⁷⁵ *Frank Shepard Co. v. Zachary P. Taylor Pub. Co.*, 180 N. Y. Supp. 122.

⁷⁶ *Chapman v. Hunt*, 254 Fed. 768.

⁷⁷ See § 5128, *infra*.

⁷⁸ *Hoover Steel Ball Co. v. Schaffer Ball Bearings Co.*, 89 N. J. Eq. 440, 106 Atl. 36.

⁷⁹ *Standard Chemical & Oil Co. v. Faircloth*, 200 Ala. 657, 77 So. 31.

⁸⁰ *Smith v. Powers*, 255 Fed. 582.

on advances made by him to the corporation, where he had knowledge of its insolvency at the time of the advances.⁸¹

§ 5086. Manner of preferring creditors. The trust-fund doctrine cannot be nullified by calling a transfer a sale where in reality a preference of a creditor.⁸²

§ 5088. Mortgages as preferences—In general. On insolvency, “claims of subsequent creditors without notice are superior and entitled to preference in payment over the holders with notice of mortgage bonds of the corporation whose only consideration was the purchase by the mortgagor corporation of its own stock, either for itself or for another.”⁸³

§ 5093. — Chattel mortgages. Where a chattel mortgage is void as to prior creditors of an insolvent corporation and is valid as to subsequent creditors after recordation, the procedure is as follows: all of the net assets of the company should be taken; from such sum should be deducted the amount of the chattel mortgage; the amount of all of the other claims should be taken and a dividend rate struck; this is the dividend rate subsequent creditors are entitled to have used; in case of prior creditors, the net assets should be taken, and the amount of all the claims including that of the chattel mortgagee should be added and a dividend rate struck; and the amount represented by the difference between these two dividend rates must be made good by the chattel mortgagee to the creditors whose claims accrued prior to the recording of the chattel mortgage.⁸⁴

§ 5097. Preferences by attachment, execution, supersedeas bond, etc. Insolvency does not preclude the acquisition of a prior lien by attachment or execution.⁸⁵ A purchaser at an execution sale of property of an insolvent corporation, where without knowledge of the insolvency, obtains rights paramount to

⁸¹ Hoover Steel Ball Co. v. Schaffer Ball Bearings Co., 89 N. J. Eq. 478, 106 Atl. 36.

⁸² Williams v. Davidson, 104 Wash. 315, 176 Pac. 334, 181 Pac. 874.

⁸³ Edgar v. Ames, 255 Fed. 835.

⁸⁴ Slater v. Slater Press, 90 N. J. Eq. 543, 107 Atl. 269.

⁸⁵ Standard Chemical & Oil Co. v. Faircloth, 200 Ala. 657, 77 So. 31.

those of other creditors.⁸⁶ If there is only one creditor of an insolvent corporation and he levies on the corporate assets, it seems that a suit to marshal assets does not lie.⁸⁷

On the other hand, in Texas, where a corporation is insolvent and has ceased to do business, an execution levied on its property and a sale thereunder convey no title as against other creditors; but if the debts are all paid a purchaser acquires a good title at the execution sale.⁸⁸

§ 5116. Preferences where banks are insolvent—Checks; reception by insolvent bank; acceptance. A depositor of a check drawn on the bank of deposit, although the deposit is not credited to the depositor, is not entitled to a preference on the bank becoming insolvent.⁸⁹

§ 5128. Statutory provisions affecting the validity of preferences—New Jersey. A corporation is insolvent, within the New Jersey statute forbidding preferences where insolvent, where there is a general inability to meet pecuniary liabilities as they mature by means of either available assets or an honest use of credit.⁹⁰ Actual suspension of business, as the term is used in the New Jersey statute relating to preferences, means more than a mere failure to meet maturing obligations as they accrue. It means an interruption of ordinary business operation evidenced by some objective features, such as cessation of manufacturing in case of a manufacturing corporation.⁹¹ Notwithstanding the statute in New Jersey forbidding preferences where a corporation is insolvent, a corporation may, if temporarily in need of funds, pledge its assets, provided the pledge is in pursuance of some financial scheme which it is reasonable to suppose will result in placing the corporation in a position of solvency.⁹²

⁸⁶ *Standard Chemical & Oil Co. v. Fairecloth*, 200 Ala. 657, 77 So. 31.

⁸⁷ *Fairecloth v. Farmers' Guano Co.*, — Ala. —, 85 So. 395.

⁸⁸ *Houston v. Shear*, — Tex. Civ. App. —, 210 S. W. 976.

⁸⁹ *Zimmerli v. Northern Bank & T. Co.*, — Wash. —, 191 Pac. 788.

⁹⁰ *Hoover Steel Ball Co. v. Scha-*

fer Ball Bearings Co., 89 N. J. Eq. 433, 105 Atl. 500; *Shoenthal v. New Jersey Gardens Co.*, — N. J. Ch. —, 103 Atl. 415.

⁹¹ *Hoover Steel Ball Co. v. Schaffer Ball Bearings Co.*, 89 N. J. Eq. 433, 105 Atl. 500.

⁹² *Hoover Steel Ball Co. v. Schaffer Ball Bearings Co.*, 89 N. J. Eq. 433, 105 Atl. 500.

§ 5129. — New York—Present statute and its effect. Under the New York statute, preferences of creditors by an insolvent corporation are void.⁹³

§ 5132. — — Transfers prohibited.⁹⁴

§ 5133. — — Notice of insolvency; bona fide purchasers. Under the provisions of the New York statute as to preferences by insolvent corporations, it is immaterial whether the preferred creditor knew of the insolvency or that the payment would operate as a preference.⁹⁵ A creditor paid in full is not a purchaser for value without notice, within the New York statute, merely because a third person surrendered the guaranty of his debt, especially where the guarantor was the president of the corporation and paid the money in its behalf.⁹⁶

§ 5135. — — Intent to prefer. There must be an intent to create a preference, to make the statute operative.⁹⁷

§ 5145. Officers of corporations as preferred creditors—Rule prohibiting preferences after insolvency. Directors in charge of an insolvent corporation have no right to apply corporate assets to their own benefit to the detriment of general creditors, and may be held to account if they do so.⁹⁸ The president of an insolvent corporation cannot prefer himself as a creditor by a transfer of property, even though with the consent of all the

⁹³ *Smith v. Powers*, 255 Fed. 582.

Application of statute, see *Griffin v. Brody, Adler & Koch Co.*, 167 N. Y. Supp. 725.

Preferential payments to creditors shortly before cessation of business are invalid. *Sherwood v. Holbrook*, 188 N. Y. App. Div. 712, 177 N. Y. Supp. 330.

⁹⁴ See § 5164, *infra*.

⁹⁵ *Smith v. Powers*, 255 Fed. 582.

⁹⁶ *Smith v. Powers*, 255 Fed. 582.

⁹⁷ *Griffin v. Wieland*, 167 N. Y. Supp. 729.

Meaning of "intent of giving preference" in New York statute, see *Karasik v. People's Trust Co.*, 252 Fed. 324, 335, quoting *Cardozo v. Brooklyn Trust Co.*, 228 Fed. 333.

⁹⁸ *Pittsburgh Steel Co. v. Davidson Hardware Co.*, 175 N. C. 450, 95 S. E. 896.

A director of an insolvent corporation, having the custody of corporate funds, cannot appropriate a large part of such assets to payment of his claims against the corporation. *Hanson v. Choynski*, 180 Cal. 275, 180 Pac. 816.

other corporate officers.⁹⁹ Directors of an insolvent company who wrongfully attempt to obtain a preference are not entitled to any preferences as against each other, as general creditors.¹

§ 5148. — Fraudulent conveyances; conversion of property. In all jurisdictions preferences of officers may be attacked for actual fraud or unfairness.²

§ 5152. — Manner of preferring officers; deeds and mortgages; advances; transfer of accounts; actions. Directors of an insolvent company cannot, in New Jersey, obtain a preference as creditors by taking a default judgment against the corporation.³ "Right of insolvent corporation to secure officers, directors or stockholders for a contemporaneous loan to the corporation" is the subject of a recent note in A. L. R.⁴

§ 5153. — Preferences to officers liable as sureties, guarantors or indorsers. Directors cannot prefer themselves where the corporation is insolvent, whether the liability sought to be protected is that of indorser, guarantor or surety.⁵ Independently of statute, officers and directors of an insolvent corporation cannot apply proceeds of sales to debts for which they are guarantors, sureties or indorsers, to the exclusion of other unsecured creditors; and sales providing for payment of such debts from the proceeds are fraudulent and may be set aside.⁶

§ 5157. Stockholders as preferred creditors—Stockholders as creditors. General creditors are entitled to be paid before stockholders can claim any portion of the assets of an insolvent corporation.⁷ Where money to make a payment on land purchased by the corporation is procured from a stockholder by a corporate

⁹⁹ *Armstrong v. Ellerslie Planting Co.*, 146 La. 559, 83 So. 830.

¹ *Shoenthal v. New Jersey Gardens Co.*, — N. J. Ch. —, 103 Atl. 415.

² *Sanborn-Cutting Co. v. Paine*, 244 Fed. 672.

³ *Shoenthal v. New Jersey Gardens Co.*, — N. J. Ch. —, 103 Atl. 415.

⁴ 5 A. L. R. 561, annotating *In re Lake Chelan Land Co.*, 257 Fed. 497, 5 A. L. R. 557.

⁵ *Hoggan v. Price River Irrigation Co.*, — Utah —, 184 Pac. 536.

⁶ *Ohio Finance Co. v. Mannington Window Glass Co.*, — W. Va. —, 103 S. E. 333.

⁷ *Perkins v. Henry Talmadge & Co.*, 147 Ga. 527, 94 S. E. 1003.

officer by fraud, and the corporation becomes insolvent, there is a constructive trust and the stockholder has a priority to recover such money as against ordinary creditors.⁸

§ 5158. — Preferred stockholders as creditors.⁹ On insolvency, creditors have priority over preferred stockholders.¹⁰ Preferred stockholders have no claim which can be satisfied until the claims of creditors, unless the preferred stock is made a prior claim by virtue, or by authority, of a statute.¹¹

§ 5160. — Right to prefer stockholders.¹² In Utah, a stockholder not a director may be preferred as a creditor even where the corporation is insolvent.¹³

§ 5164. Statutory prohibitions against preferences to officers and stockholders. A mortgage is a "transfer" within the meaning of the New York statute forbidding transfers of corporate property to officers except for full value where the corporation has refused to pay any of its notes.¹⁴ The New York statute prohibiting transfers to officers after refusal to pay any obligation when due, makes invalid a lease to a wife of the president for a nominal sum, where she sublet it for a large sum.¹⁵ The word "obligations" in the New York statute providing that no corporation which shall have refused to pay any of its notes or other "obligations," etc., is no broader than the term "evidences of debt"; and while it does not include open accounts it does include contract obligations.¹⁶

§ 5165. Recovery of invalid preferences; accounting—Remedies. If stockholders sell their stock to the corporation after knowledge of its insolvency, such payments may be recovered

⁸ Biddle v. Biddle, 202 Mich. 160, 168 N. W. 92.

⁹ See also § 3628, supra.

¹⁰ Armstrong v. Union Trust & Savings Bank, 248 Fed. 268.

On insolvency, the owners of preferred stock cannot participate until after creditors are paid. Booth v. Union Fibre Co., 142 Minn. 127, 171 N. W. 307.

¹¹ Hewitt v. Linnhaven Orchard

Co., 90 Ore. 1, 174 Pac. 616.

¹² See also § 3645, supra.

¹³ Hoggan v. Price River Irrigation Co., — Utah —, 184 Pac. 536.

¹⁴ Karasik v. People's Trust Co., 252 Fed. 324, 334.

¹⁵ Anton Larsen & Son v. Newmark & Davis, 182 N. Y. App. Div. 724, 170 N. Y. Supp. 268.

¹⁶ Karasik v. People's Trust Co., 252 Fed. 324, 335.

by the receiver.¹⁷ An unpaid creditor of an insolvent corporation cannot sue one whose claim has been wrongfully paid, to recover the amount of the improper preference, to the extent of the claim of the unpaid creditor.¹⁸ An action to recover payments to officers or stockholders as preferential is one at law so as to entitle plaintiff to a jury.¹⁹ Equity will interpose, at the suit of a creditor of an insolvent corporation, to defeat a preference of a director as a creditor, where relief has been unsuccessfully sought in the bankruptcy court, the only legal tribunal with power to defeat such a preference.²⁰

§ 5168. — Limitations; estoppel.²¹

§ 5169. — Parties. In a suit by a creditor of an insolvent corporation to defeat a preference by a director of himself as a creditor in regard to money held by him in trust, the other directors are necessary parties.²²

§ 5173. — Judgments; amounts recoverable. If a creditor purchases all the assets of an insolvent corporation with knowledge of its insolvency, and pays certain other claims against the corporation, but not all of them, as a part of the consideration, the decree, in an action to set aside the transfer, should not be for the value of all the corporate assets received but only for the value in excess of his pro rata share as creditor in the corporate assets.²³

§ 5174. Set-off by debtors of insolvent corporations—Right of set-off in general. The right of set-off against an insolvent company is governed by the state of things at the time of insolvency rather than by conditions thereafter created.²⁴ As against the debt of an insolvent bank to a surety company, the

¹⁷ Holyfield v. Davis, 139 Ark. 479, 214 S. W. 53.

¹⁸ P. B. Yates Mach. Co. v. La-kin, — Wash. —, 192 Pac. 982.

¹⁹ Rottenberg v. Englander, 185 N. Y. App. Div. 1, 172 N. Y. Supp. 641.

²⁰ Hanson v. Choynski, 180 Cal. 275, 180 Pac. 816.

²¹ See § 5062, *supra*.

²² Hanson v. Choynski, 180 Cal. 275, 180 Pac. 816.

²³ Williams v. Davidson, 104 Wash. 315, 176 Pac. 334, 181 Pac. 874.

²⁴ Chipley State Bank v. McNeill, 77 Fla. 827, 82 So. 292.

bank cannot set off a dividend on stock of the surety company held by the bank.²⁵ Where dividends on stock of another company accrue and are paid while the stockholding company is in the hands of a receiver, the corporation declaring the dividends cannot set off a debt due by the insolvent against an action by the receiver to recover such dividends.²⁶

§ 5178. — Insolvent banks. On insolvency of a bank, deposits may be set off against debts.²⁷

§ 5179. — Set-off by stockholders. A stockholder indebted to an insolvent corporation for unpaid subscription cannot set off a debt due him by the corporation.²⁸ The set-off provision of the Federal Bankruptcy Act does not apply.²⁹

The claim of a creditor stockholder should not be allowed until his stock indebtedness to the bankrupt has been collected by plenary suit.³⁰ But it is held that where the holder of unpaid stock is a creditor of a bankrupt corporation, allowance of his claim cannot be conditioned on payment of the amount due on his stock where the assessment has not been judicially ascertained.³¹

§ 5181. — Termination of right; claims against corporations assigned to debtors. Claims purchased or acquired after failure

²⁵ *In re People's Surety Co.*, 186 N. Y. App. Div. 663, 175 N. Y. Supp. 74.

²⁶ *Chipley State Bank v. McNeill*, 77 Fla. 827, 82 So. 292.

²⁷ *Funk & Son v. Young*, 138 Ark. 38, 5 A. L. R. 79, 210 S. W. 143; *Chipley State Bank v. McNeill*, 77 Fla. 827, 82 So. 292.

²⁸ *In re La Jolla Lumber & Mill Co.*, 243 Fed. 1004; *Cooper v. Eastern Horse & Mule Co.*, — Del. Ch. —, 110 Atl. 666; *Vaughan-Robertson Drug Co. v. Grimes-Mills Drug Co.*, 173 N. C. 502, 92 S. E. 376.

A depositor in a bank sued as a stockholder of the insolvent bank

for corporate debts cannot set off his deposit, under the present statutes of Georgia. *Swicord v. Crawford*, 148 Ga. 719, 98 S. E. 343.

²⁹ *Cochran v. Monteith*, — Tex. Civ. App. —, 221 S. W. 1055.

³⁰ *Boatmen's Bank v. Laws*, 257 Fed. 299; *In re Caledonia Coal Co.*, 254 Fed. 742, 746.

If a stockholder presents a claim against the corporation in bankruptcy, he cannot recover thereon, as against other creditors, until he has first paid the amount payable on his stock. *In re Caledonia Coal Co.*, 254 Fed. 742.

³¹ *Moise v. Scheibel*, 245 Fed. 546.

of an insolvent bank cannot be set off against a debt due the bank.³²

II. BANKRUPTCY

§ 5184. Rights of corporations to become bankrupts; voluntary proceedings. An electric light company may be adjudged a bankrupt,³³ and a gas company is entitled to go into bankruptcy although a majority of its stock is held by a holding company and a suit is pending to enjoin an increase in the charge for gas.³⁴ An electric street railway is not a "railroad" within the bankruptcy act excepting railroad companies from those who may become bankrupt.³⁵ Stockholders may intervene, in case of fraud, to contest a voluntary petition in bankruptcy filed by officers on behalf of the corporation.³⁶ Appointment of a temporary receiver in a state court does not preclude directors from filing a voluntary petition in bankruptcy.³⁷

§ 5189. Involuntary bankruptcy proceedings against corporations—Mining corporations. A corporation chartered to mine and deal in coal but which has discontinued mining and purchasing coal and is engaged solely in transporting coal for others is not a corporation "engaged principally in * * * mining or mercantile pursuits" so as to be subject to be declared an involuntary bankrupt.³⁸

§ 5194. Acts of bankruptcy—Transfers of property with fraudulent intent; preferences. There is no fraudulent transfer of property, such as to constitute an act of bankruptcy, where the sole stockholder who transferred corporate property, had no knowledge there were any corporate debts.³⁹

§ 5195. — Assignment for benefit of creditors.⁴⁰

³² Smedley v. Mauney, 141 Ark. 16, 215 S. W. 890.

³³ In re Grafton Gas & Electric Light Co., 253 Fed. 668.

³⁴ City of Holland v. Holland City Gas Co., 257 Fed. 679.

³⁵ In re Grafton Gas & Electric Light Co., 253 Fed. 668.

³⁶ Zeiting v. Hargadine-McKit-

trick Dry Goods Co., 244 Fed. 719.

³⁷ In re Dressler Producing Corporation, 262 Fed. 257.

³⁸ In re C. Jutte & Co., 266 Fed. 357.

³⁹ In re M. S. Fersko, Inc., 250 Fed. 357.

⁴⁰ Assignment for benefit of creditors as act of bankruptcy,

§ 5196. — **Receiverships.** Consenting to the appointment of a receiver is not equivalent to having “applied” for a receiver, so as to be an act of bankruptcy.⁴¹ Application by stockholders and creditors for a receiver is not an act of bankruptcy of the corporation.⁴²

§ 5197. — **Admission of inability to pay debts.** A letter written by a clerk by authority of the directors advising a creditor to institute bankruptcy proceedings, and stating that if brought the company would admit its insolvency, is not such an unqualified admission as to constitute an act of bankruptcy.⁴³ Under the Maine statute forbidding corporations to part with any of their property “essential to the conduct” of the corporate business, except with the consent of stockholders given at a meeting, a corporation cannot make an unqualified admission such as to constitute an act of bankruptcy without consent of the stockholders.⁴⁴

§ 5198. **Jurisdiction of proceedings.**⁴⁵ In case of a bankrupt corporation, appearance by a stockholder to contest a petition by the trustee in bankruptcy for an assessment on all stock not fully paid for, does not confer jurisdiction on the bankruptcy court to adjudicate his personal liability for such assessment.⁴⁶

§ 5199. **Estoppel preventing petition for bankruptcy.** It is not a fraud for directors to institute voluntary bankruptcy proceedings although a stockholder has commenced a suit for dissolution in a state court.⁴⁷

§ 5200. **Pleading.** Specifications of objection to a bankrupt’s discharge, where made by a corporation, must be signed

see *Moody-Hormann-Boelhauwe v. Clinton Wire Cloth Co.*, 246 Fed. 653.

⁴¹ *In re Big Pines Lime & Transportation Co.*, 257 Fed. 141.

⁴² *Hansen v. Uniform Seamless Wire Co.*, 243 Fed. 177.

⁴³ *In re Standard Shipyard Co.*, 262 Fed. 522.

⁴⁴ *In re Standard Shipyard Co.*, 262 Fed. 522.

⁴⁵ See also § 403, *supra*.

⁴⁶ *Bergdoll v. Harrigan*, 263 Fed. 279, *rev’g in part* 260 Fed. 234.

⁴⁷ *In re Dressler Producing Corporation*, 262 Fed. 257.

by the corporation by having its seal affixed by proper authority.⁴⁸

§ 5203. Claims.⁴⁹ A corporate contract illegal because contrary to statute cannot be enforced as a claim against a bankrupt although it has had the benefit of its performance.⁵⁰ A purchaser of corporate property within four months prior to bankruptcy cannot be compelled to pay a second time to the trustee in bankruptcy because in making his first payment he complied with a request of the president and general manager and applied a portion of the price to the discharge of their personal debts incurred for the benefit of the corporation.⁵¹

§ 5204. Effect of bankruptcy.⁵² Bankruptcy does not prevent election of corporate officers while the corporate affairs are being conducted in the bankruptcy court.⁵³ Where a creditor agreed to receive his pay out of the net earnings of the corporation, the filing thereafter of a voluntary petition in bankruptcy is not a breach of the contract entitling the creditor to rescind.⁵⁴

§ 5205. Powers and duties of trustees.⁵⁵ A trustee in bankruptcy is entitled to possession of corporate property notwithstanding the prior appointment of a receiver for the insolvent company in a state court.⁵⁶ A trustee in bankruptcy may sue to recover assets of the bankrupt corporation unlawfully diverted, where necessary to liquidate claims of creditors.⁵⁷ The principal

⁴⁸ In re Abramowitz, 253 Fed. 299.

⁴⁹ Claim for unpaid subscription as a contingent claim, where stockholder is a bankrupt, see In re Thompson, 257 Fed. 140.

⁵⁰ In re Springfield Realty Co., 257 Fed. 785.

⁵¹ Doughty v. Moors, — Cal. App. —, 183 Pac. 199.

⁵² Mortgage to secure bonds of irrigation company, rights under, where company became bankrupt, see First Trust & Savings Bank v. Bitter Root Valley Irrigation Co., 251 Fed. 320.

⁵³ In re O'Gara Coal Co., 260 Fed. 742.

⁵⁴ In re 35% Automobile Supply Co., 247 Fed. 377.

⁵⁵ Security for costs, under New York statute, in action by trustee in bankruptcy to recover on a stock subscription, see Allen v. McCormick, 110 N. Y. Misc. 254, 180 N. Y. Supp. 116.

⁵⁶ Brown v. Crawford, 254 Fed. 146.

⁵⁷ Miley v. Heaney, 168 Wis. 58, 169 N. W. 64.

place of business of the bankrupt corporation rather than the residence of the trustee fixes the venue of actions by the trustee.⁵⁸ Bankruptcy court has no jurisdiction of a suit by a trustee in bankruptcy to enforce collection of unpaid subscriptions to stock in a single suit, where the debts are unconditionally due by the terms of the subscription contract.⁵⁹ Where the bankrupt is a corporation, summary proceedings may lie to recover property of the corporation in possession of an officer thereof who makes no personal claim to the property; but if he sets up title in himself a plenary suit is necessary.⁶⁰ A decree against a corporation subsequently adjudicated a bankrupt is conclusive against the trustee in bankruptcy and the general creditors he represents.⁶¹

⁵⁸ *Allen v. McCormick*, 110 N. Y. Misc. 254, 180 N. Y. Supp. 116.

⁶⁰ *In re Joseph R. Marquette, Jr., Inc.*, 254 Fed. 419.

⁵⁹ *Kelley v. Gill*, 245 U. S. 116, 62 L. Ed. 185, *aff'd* *Kelly v. Aarons*, 238 Fed. 996.

⁶¹ *Rader v. Star Mill & Elevator Co.*, 258 Fed. 599.

CHAPTER 63

RECEIVERS

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I. GENERAL CONSIDERATIONS

§ 5210. Number of receivers.¹

II. APPOINTMENT

A. Jurisdiction

§ 5211. **In general.** Where a federal court decides to appoint a receiver for a corporation, and then the parties agree to a plan of operation under direction of the court without a receiver, the court does not lose jurisdiction of the case by the lapse of several years during which the plan was being tried out.²

§ 5214. **Equity courts.** In Illinois it is held that courts of equity have no general power to appoint receivers of corporations, and the general rule is that they can appoint receivers only where expressly authorized by the statutes.³ In Oklahoma, it is held that a court of equity has inherent power to appoint a receiver upon the petition of minority stockholders.⁴

§ 5216. **Statutory jurisdiction.** In case of banks, the power to appoint a receiver for a bank is often vested in a state examiner or state banking board.⁵

§ 5217. **Federal courts and conflicting jurisdiction.**⁶ The rule that the court first acquiring jurisdiction retains it, as between state and federal courts, applies to the appointment of receivers.⁷

A federal court in the state where the corporation was created has jurisdiction of a suit to appoint a receiver under a state

¹ See § 5239, *infra*.

² *City of Toledo v. Toledo Railways & Light Co.*, 259 Fed. 450.

³ *Blanchard Bro. & Lane v. S. G. Gay Co.*, 289 Ill. 413, 124 N. E. 616.

⁴ *Union State Bank v. Mueller*, — Okla. —, 172 Pac. 650.

⁵ See *State ex rel. Lofthus v. Langer*, — N. D. —, 177 N. W. 408.

⁶ Conflict of jurisdiction between

state and federal courts as to appointment of receiver, see *Wheeler v. Badenhausen Co.*, 260 Fed. 991.

Conflict between federal and state courts in receivership proceedings, see *Phillips v. Noel Const. Co.*, 266 Fed. 603; *Cavagnaro v. Indian Tire & Rubber Co.*, 90 N. J. Eq. 532, 107 Atl. 643.

⁷ *Ward v. Foulkrod*, 264 Fed.

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statute, in case of the requisite diversity of citizenship and sufficiency of amount involved.⁸ A federal court outside the state where the corporation was created, but in the state where the principal business is conducted through subsidiary corporations, has jurisdiction to appoint a receiver.⁹ A suit to appoint a receiver to protect corporate assets is one of a local nature, under the federal statutes, and cannot be brought in a district where the corporation is not domiciled and has no property of a fixed nature.¹⁰ Objection to the jurisdiction of a federal court to appoint a receiver may be waived by failure of the corporation to object.¹¹

A state court may appoint a receiver for an insolvent corporation or one conducting its business at a great loss, where grounds for a receiver in that state, although its assets have been for some time under the control of a receiver appointed in another state by a federal court.¹² The fact that a federal court has taken over the administration of the affairs of a corporation in a general administration suit, and appointed a receiver, does not preclude proceedings under the New Jersey statute in a state court to wind up the corporation, since the relief which may be granted in the federal court is not as comprehensive as that which may be awarded in the state court.¹³

A state receivership must give way to federal bankruptcy proceedings.¹⁴

§ 5222. Power to appoint as limited to incidental relief. A receiver cannot be appointed except as incidental to other re-

⁸ *Adler v. Campeche Laguna Corporation*, 257 Fed. 789.

Stockholders may obtain the appointment of a receiver in the federal court, under the New Jersey statutes, where the corporation is insolvent. *Kessler v. William Necker, Inc.*, 258 Fed. 654.

⁹ *Scattergood v. American Pipe & Construction Co.*, 249 Fed. 23.

¹⁰ *Primos Chemical Co. v. Fulton Steel Corporation*, 254 Fed. 454.

¹¹ *Kessler v. William Necker, Inc.*, 258 Fed. 654.

¹² *Hitchcock v. American Pipe*

& Construction Co., 89 N. J. Eq. 440, 105 Atl. 655. To same effect, *Michel v. William Necker, Inc.*, 90 N. J. Eq. 171, 106 Atl. 449.

¹³ *Michel v. William Necker, Inc.*, 90 N. J. Eq. 171, 106 Atl. 449, where difference between receivers and the power to dissolve, in the two courts, is referred to as material.

¹⁴ *Gealey v. South Side Trust Co.*, 249 Fed. 189, holding, however, that receiver should not turn over property without order of state court.

Bankruptcy proceedings take

lief.¹⁵ He cannot be appointed merely to take the place of the management of the corporation, to act for an indefinite time, i. e., merely prescribe a moratorium in favor of a corporation.¹⁶

B. Who May Obtain Appointment

§ 5226. Stockholder.¹⁷

§ 5228. Creditor. A receiver may be appointed in a creditor's suit to set aside a fraudulent conveyance of all its property by an insolvent corporation.¹⁸ A pending stockholders' suit in a federal court to enforce corporate rights and incidentally asking for a receiver does not bar a suit by a creditor for a receiver.¹⁹

§ 5231. Corporation itself. A corporation cannot sue to marshal its own assets and for a receiver, over the objections of creditors or stockholders.²⁰

C. Propriety of Appointment

§ 5234. Discretion of court.²¹ A receiver should not be appointed in a doubtful case.²² Where the appointment of a receiver will do the person seeking a receivership no good, and it will do a great injury to others, a receivership should be denied.²³ Where, after dissolution of a corporation by lapse

precedence over the prior appointment of a receiver in a state court, but the receiver should not wind up the receivership and turn over the property without first applying to the state court for leave to do so. *Cudahy Packing Co. v. New Jersey Dairy Products Co.*, — N. J. Ch., —, 107 Atl. 147.

¹⁵ *Hitchcock v. American Pipe & Construction Co.*, 89 N. J. Eq. 440, 105 Atl. 655; *Alto Cotton Oil & Manufacturing Co. v. Berryman*, — Tex. Civ. App., —, 218 S. W. 513.

¹⁶ *Hitchcock v. American Pipe & Construction Co.*, 89 N. J. Eq. 440, 105 Atl. 655.

¹⁷ See § 5234, *infra*.

¹⁸ *Biehn v. Aetna Inv. Co.*, — Wash., —, 188 Pac. 489.

¹⁹ *Adler v. Seaman*, 266 Fed. 828.

²⁰ *Bartlett v. Taylor*, 148 Ga. 110, 98 S. E. 491, where directors of bank applied for a receiver to prevent a run on the bank.

²¹ General rules as to propriety of appointment of a receiver, see *Apalachicola Northern R. Co. v. Sommers*, — Fla., —, 85 So. 361.

²² *Davis v. Hudgins*, — Tex. Civ. App., —, 225 S. W. 73.

²³ *Langer v. Fargo Mercantile Co.*, — N. D., —, 174 N. W. 90.

of time, the statutory trustees convey the assets to a new corporation, a receiver should not be appointed for the new corporation where the receivership is wholly unnecessary.²⁴

Courts are reluctant to appoint a receiver, at the suit of stockholders, because of corporate mismanagement or for the purpose merely of preserving the assets.²⁵ A stockholder cannot obtain the appointment of a receiver merely because the corporation which is solvent will be endangered by creditors who may obtain judgments and attempt to collect them, and that the corporate officers are powerless to obtain money to prevent such threatened danger, at least where the receiver would be in no better position to obtain money.²⁶

§ 5235. As dependent upon nature of corporation. Ordinarily a receiver cannot be appointed for a religious corporation.²⁷

§ 5239. Two or more receiverships at same time. A receiver should not be appointed where there is already a general receiver and there is no necessity for another receiver.²⁸ A corporate receivership is properly extended to a foreclosure suit and the appointment of a separate receiver refused, in a proper case.²⁹

D. Grounds

§ 5240. In general. There "is a clear distinction between a receivership on the ground of insolvency and a receivership for conservation of assets and rehabilitation of creditors."³⁰ A receiver of a corporation may be appointed in aid of an interlocutory injunction preventing a railroad company from discontinuing operations.³¹

²⁴ *Langer v. Fargo Mercantile Co.*, — N. D. —, 174 N. W. 90.

²⁵ *Blanchard Bro. & Lane v. S. G. Gay Co.*, 289 Ill. 413, 124 N. E. 616.

²⁶ *Blanchard Bro. & Lane v. S. G. Gay Co.*, 289 Ill. 413, 124 N. E. 616.

²⁷ *King v. Smith*, 106 Kan. 624, 189 Pac. 147.

²⁸ *Adler v. Seaman*, 266 Fed. 828.

²⁹ *Bankers' Trust Co. v. Missouri, K. & T. Ry. Co.*, 251 Fed. 789.

³⁰ *Wheeler v. Dadenhausen Co.*, 260 Fed. 991, 995.

³¹ *Milltown Lumber Co. v. Milltown*, — Ga. —, 102 S. E. 435.

§ 5244. Dissensions or disagreements among officers or stockholders. Minority stockholders are not entitled to a receiver for a solvent corporation merely because they are not satisfied with the management.³² A receiver should not be appointed at the instance of minority stockholders, merely because majority stockholders stifle the minority in the management, where the corporation is very successful and a receivership would injure all concerned, but instead jurisdiction of the case should be retained with leave to minority stockholders to apply for relief if deemed necessary.³³ Where two brothers owned practically all the stock of a corporation, a receiver should not be appointed at the instance of one of them, to carry on the business of the corporation, because of disagreements between the brothers, where they can administer the business more economically and better than a receiver.³⁴

§ 5246. Misconduct or mismanagement of directors, officers or majority stockholders. Misconduct of officers of a solvent corporation ordinarily is not of itself a ground for a receiver.³⁵ A minority stockholder cannot obtain a receiver because of mismanagement unless fraud of the directors appears.³⁶ A receiver should not be appointed at the instance of a minority stockholder merely because of isolated or occasional dishonest or criminal acts of the majority stockholder.³⁷ Fraud of majority stockholders in handling the corporate assets is ground for a temporary receiver in a suit by minority stockholders.³⁸

In case of a one man corporation, a receiver is properly appointed where the stockholder turned over all his assets to the corporation in return for its stock, part of which he fraudulently transferred to his wife to defeat his creditors.³⁹

§ 5249. Losing business.⁴⁰

³² *Beeler v. Standard Inv. Co.*, 107 Wash. 442, 5 A. L. R. 363, 181 Pac. 896.

³³ *South Norfolk Land Co. v. Tebault*, 124 Va. 667, 98 S. E. 679.

³⁴ *Yantis v. Gulf Coast Rice Farm Co.*, 144 La. 486, 80 So. 667.

³⁵ *Riordan v. Baldwin*, — Ga. —, 104 S. E. 204.

³⁶ *Nobis v. Nobis*, 193 N. Y. App.

Div. 218, 183 N. Y. Supp. 726.

³⁷ *Kahan v. Alaska Junk Co.*, — Wash. —, 189 Pac. 262.

³⁸ See *Bates v. Werries*, 198 Mo. App. 209, 199 S. W. 758, where receiver pendente lite was appointed.

³⁹ *Harnau v. Haight*, 209 Mich. 604, 177 N. W. 281.

⁴⁰ What constitutes doing business at great loss so that business

§ 5250. **Insolvency—In general.** Under the Delaware statute, insolvency alone is ground for a receivership.⁴¹ Generally, however, insolvency alone is not ground for a receivership.⁴²

§ 5251. — **Imminent danger of insolvency.** Minority stockholders may obtain the appointment of a receiver to wind up the corporation where the officers have plundered it or so mismanaged it as to put it on the verge of bankruptcy, where its purposes are no longer attainable, and where there is no other adequate remedy.⁴³ Where the property of a corporation is being mismanaged, and is in danger of being lost to the stockholders through collusion and fraud of its officers, a receiver is properly appointed under a statute making imminent danger of insolvency ground for a receiver.⁴⁴

§ 5253. — **What constitutes insolvency.**⁴⁵

§ 5257. **Danger of loss pendente lite.** A temporary receivership in a pending suit, to take possession of corporate assets, is proper where it is made to appear *prima facie* that the assets are in danger of dissipation or concealment.⁴⁶

E. Grounds for Refusing

§ 5259. **In general.** A judgment creditor's suit, brought in behalf of all the creditors, for a receiver for a corporation, cannot

be conducted with safety to the public and advantage to the stockholders, warranting the appointment of a receiver, under the New Jersey statutes, see *Hitchcock v. American Pipe & Construction Co.*, 89 N. J. Eq. 440, 105 Atl. 655.

⁴¹ *Adler v. Campeche Laguna Corporation*, 257 Fed. 789.

In Delaware, since the statute expressly provides that the appointment of a receiver whenever a corporation shall be insolvent, is discretionary, it is proper to refuse a receivership where no mismanagement is alleged and the appointment of a receiver will serve no good purpose. *Sill v. Kentucky*

Coal & Timber Development Co., 259 Fed. 366.

⁴² *Adler v. Campeche Laguna Corporation*, 257 Fed. 789.

⁴³ *Goodwin v. Milwaukee Lithographing Co.*, — Wis. —, 177 N. W. 618.

⁴⁴ *Kahle v. Industrial Loan & Investment Co.*, 103 Wash. 273, 174 Pac. 23.

⁴⁵ What constitutes insolvency warranting the appointment of a receiver under the New Jersey statutes, see *Hitchcock v. American Pipe & Construction Co.*, 89 N. J. Eq. 440, 105 Atl. 655, and see §§ 5008, 5128, *supra*.

⁴⁶ *Davison v. Davison Realty Co.*, 186 Iowa 27, 172 N. W. 165.

not be defeated by paying only the judgment belonging to plaintiff.⁴⁷

§ 5260. Absence of necessity.⁴⁸ The appointment of a receiver, where the corporation is solvent, in an equitable suit to reach certain corporate assets, will be refused where there is no danger of loss.⁴⁹

§ 5261. Absence of benefit.⁵⁰

§ 5262. Other adequate remedy—In general. A receiver should not be appointed where the remedy by injunction is adequate.⁵¹

§ 5263. — Remedy within the corporation. A receiver should not be appointed where it is not shown that complainant, a minority stockholder, has exhausted his remedies within the corporation nor instituted suitable criminal proceedings.⁵²

§ 5266. Absence of assets. The fact that an insolvent corporation has transferred all its assets to a stockholder does not show that it has no assets justifying the appointment of a receiver, in view of the trust-fund doctrine.⁵³ Presence of assets in the state is not a prerequisite to the appointment of a receiver, under the Delaware statutes, in case of insolvency.⁵⁴

G. Procedure and Subsequent Steps

§ 5269. General rules. There is no impropriety in having the attorney for complainant act as the attorney for the receiver, where there are no creditors and no diversity between

⁴⁷ *Parten v. Southern Colonization Co.*, — Minn. —, 178 N. W. 744.

⁴⁸ See also § 5234, *supra*.

⁴⁹ *American Manganese Steel Co. v. Alaska Mines Corporation*, 250 Fed. 614.

⁵⁰ See § 5234, *supra*.

⁵¹ *Mitchell v. Banco de Londres y Mexico*, 192 N. Y. App. Div. 720, 183 N. Y. Supp. 446; *Bordages v. Burnett*, — Tex. Civ. App. —, 221

S. W. 326; *Merchants' Transfer Co. v. Hildebrand*, — Tex. Civ. App. —, 200 S. W. 551; *Kahan v. Alaska Junk Co.*, — Wash. —, 189 Pac. 262.

⁵² *Kahan v. Alaska Junk Co.*, — Wash. —, 188 Pac. 489.

⁵³ *Biehn v. Aetna Inv. Co.*, — Wash. —, 188 Pac. 489.

⁵⁴ *Adler v. Campeche Laguna Corporation*, 257 Fed. 789.

stockholders.⁵⁵ A foreclosure suit may be consolidated with a receivership proceeding in a proper case.⁵⁶ A receivership ordinarily should not be extended to another suit where the main purpose is, or result would be, to take up litigation against corporate officials.⁵⁷ The right of a corporation to attack as unconstitutional a statute providing for the appointment of receivers for corporations without notice is not waived by the fact that the corporation was created under the statute containing such provision.⁵⁸

§ 5270. Time for appointment. A receiver may be appointed before service of process on the corporation.⁵⁹

§ 5272. Pleadings and motion papers. A receiver should not be appointed ex parte on affidavits on information and belief.⁶⁰ A bill by a stockholder seeking a receiver on the ground of insolvency is not within rule 27 of the federal equity rules as to pleading in actions by stockholders.⁶¹ Receivers for a street railroad may petition in the original suit to restrain a city from forfeiting the franchise.⁶²

§ 5274. Parties defendant and intervention.⁶³ Stockholders are not necessary parties to a suit to appoint a receiver.⁶⁴ It is discretionary with the court whether to permit a stockholder to file a petition in the receivership suit challenging the validity of the receivership, and seeking an accounting from and removal of the receivers, or to relegate the stockholder to an independent action.⁶⁵ A stockholder may intervene in a receivership in a

⁵⁵ Cahall v. Lofland, — Del. Ch. —, 107 Atl. 769.

⁵⁶ Bankers' Trust Co. v. Missouri, K. & T. Ry. Co., 251 Fed. 789.

⁵⁷ Adler v. Seaman, 266 Fed. 828.

⁵⁸ Morse v. Metropolitan S. S. Co., 88 N. J. L. 325, 102 Atl. 524, aff'g — N. J. Ch. —, 100 Atl. 219.

⁵⁹ Greenfield v. Hill City Land, Loan & Lumber Co., 141 Minn. 393, 170 N. W. 343.

⁶⁰ Alto Cotton Oil & Manufacturing Co. v. Berryman, — Tex.

Civ. App. —, 218 S. W. 513.

⁶¹ Adler v. Campeche Laguna Corporation, 257 Fed. 789.

⁶² Gas & Electric Securities Co. v. Manhattan & Queens Traction Co., 266 Fed. 625.

⁶³ Intervention in suit for receiver, see generally Adler v. Seaman, 266 Fed. 828.

⁶⁴ Greenfield v. Hill City Land, Loan & Lumber Co., 141 Minn. 393, 170 N. W. 343.

⁶⁵ Nevin v. Pacific Coast & Norway Packing Co., 105 Wash. 192, 177 Pac. 739.

federal court of another state to question the jurisdiction of the court;⁶⁶ but a stockholder cannot intervene to question jurisdiction where the corporation has voluntarily appeared.⁶⁷ Where a defendant corporation admits its insolvency and consents to a receiver, stockholders cannot intervene as of right to vacate the receivership.⁶⁸

The right of a stockholder to intervene in an action for a receivership may be lost by laches in applying.⁶⁹ An intervener coming in four years after the appointment of a receiver cannot attack the jurisdiction of the court to appoint the receiver or to authorize him to issue certificates of indebtedness.⁷⁰

§ 5275. Order or decree. An order appointing receivers may restrain stockholders from meeting and electing new directors,⁷¹ and may enjoin city officers from enforcing a forfeiture of the street franchise.⁷² Counsel fees may be allowed stockholders in their suit for a receivership.⁷³

§ 5277. Waiver of objections to appointment.⁷⁴

§ 5278. Collateral attack. A petition by a receiver for the assessment of stockholders cannot be resisted by a collateral attack on the appointment of the receiver, unless the invalidity of the appointment appears on the face of the record.⁷⁵ Five years after the appointment of a receiver in an action to which the stockholders were made parties, stockholders cannot for the first time collaterally attack the appointment of the receiver on the ground that the court had no jurisdiction to appoint a receiver at the instance of the corporation itself.⁷⁶

⁶⁶ *Hitchcock v. American Pipe & Construction Co.*, 89 N. J. Eq. 440, 105 Atl. 655.

⁶⁷ *Scattergood v. American Pipe & Construction Co.*, 249 Fed. 23.

⁶⁸ *Cole v. Seaman*, 266 Fed. 846.

⁶⁹ *Nevin v. Pacific Coast & Norway Packing Co.*, 105 Wash. 192, 177 Pac. 739, where delay was three years after appointment of receiver.

⁷⁰ *Pillinger v. Beaty*, 265 Fed. 551.

⁷¹ *Graselli Chemical Co. v.*

Aetna Explosives Co., 252 Fed. 456.

⁷² *Westinghouse Elec. & Mfg. Co. v. Richmond Light & Railroad Co.*, 267 Fed. 490.

⁷³ *Shannon v. Shepard Mfg. Co.*, 230 Mass. 224, 119 N. E. 768.

⁷⁴ See § 5274, *supra*.

⁷⁵ *Greenfield v. Hill City Land, Loan & Lumber Co.*, 141 Minn. 393, 170 N. W. 343.

⁷⁶ *Bartlett v. Taylor*, 148 Ga. 110, 98 S. E. 491.

§ 5279. **Duration, removal and discharge.** A creditor is entitled to have the receiver discharged where his appointment was merely to defeat the creditor's claim.⁷⁷ The court in charge of a receivership has no jurisdiction as to taxes imposed after the termination of the receivership.⁷⁸

III. EFFECT OF RECEIVERSHIP

§ 5280. **General rules.** A receivership does not affect liability for taxes.⁷⁹

§ 5282. **Vesting title in receiver.**⁸⁰ In Ohio the effect of the appointment of a receiver by the state court and his seizure of the corporate property is to fasten the claims of creditors upon it and give the receiver control over it as effectually as the creditors would have held it by attachment or levy.⁸¹

§ 5283. **Right to possession.** Property of a corporation will not be permitted to be taken out of the hands of its receiver, and his possession may be protected by summary proceedings.⁸²

§ 5284. **Rights of stockholders.** A stockholders' suit to recover corporate assets from corporate officers is properly permitted although the corporation is in the hands of a receiver, where leave is secured from the court appointing the receiver, and the receiver is joined as a party.⁸³

§ 5285. **Rights and powers of officers.** Appointment of a receiver does not necessarily invalidate subsequent contracts made by the corporation.⁸⁴ After a receiver is appointed for an insolvent corporation, it cannot, as lessee, make a contract

⁷⁷ Peterson v. Daniels, — Colo. —, 192 Pac. 494.

⁷⁸ Spencer v. Babylon R. Co., 250 Fed. 24.

⁷⁹ See § 5370, *infra*.

⁸⁰ Appointment of receiver as "change of title or possession," within forfeiture clause of insurance policy, see Bowling v. Continental Ins. Co., — W. Va. —, 103 S. E. 285.

⁸¹ In re Bettman-Johnson Co., 250 Fed. 657.

⁸² Wood v. National Corporation, 265 Fed. 791.

⁸³ Adler v. Seaman, 266 Fed. 828.

⁸⁴ Standard Roller Bearing Co. v. Hess-Bright Mfg. Co., 264 Fed. 516.

modifying the lease.⁸⁵ The appointment of a receiver bars the right of directors to file a voluntary petition in bankruptcy.⁸⁶ Where an order appointing a receiver forbids the corporate officers and directors to exercise any of their powers, acts subsequently performed by the directors are not binding on the corporation.⁸⁷

§ 5286. Rights of creditors or lienholders. Liens are not divested by a receivership.⁸⁸ The title of the receiver is subject to all liens and equities, whether created by operation of law or by the act or contract of the corporation, which existed against the property at the time of his appointment.⁸⁹ Appointment of a receiver does not prevent a creditor from thereafter filing a lien against the corporation.⁹⁰ A receivership does not prevent foreclosing a mortgage on the corporate property, nor should a foreclosure be enjoined because thereof.⁹¹ Under the Rhode Island statutes, the appointment of a receiver does not vacate an attachment.⁹² The appointment of a receiver bars the right of a pledgee of stock to sue to compel directors and stockholders to restore corporate assets improperly withdrawn.⁹³

§ 5288. Existing contracts—In general. Insolvency of a corporation and appointment of a receiver does not terminate its contracts for supplies.⁹⁴

⁸⁵ *Gulf Compress Co. v. Merchants' Cotton Press & Storage Co.*, 265 Fed. 199.

⁸⁶ *Cavagnaro v. Indian Tire & Rubber Co.*, 90 N. J. Eq. 532, 107 Atl. 643.

⁸⁷ *Cavagnaro v. Indian Tire & Rubber Co.*, 90 N. J. Eq. 532, 107 Atl. 643.

⁸⁸ *Fletcher American Nat. Bank v. McDermid*, — Ind. App. —, 128 N. E. 685.

⁸⁹ *Smith & Furbush Mach. Co. v. Huycke*, — Okla. —, 177 Pac. 919, applying rule to lien on proceeds of insurance.

A receiver takes notes subject to all defenses which might have been interposed against the corpo-

ration. *Bailey v. State*, — Okla. —, 179 Pac. 615.

⁹⁰ *Brown v. Hunt & Mottet Co.*, — Wash. —, 191 Pac. 860.

⁹¹ *Stuard Lumber Co. v. Taylor*, — Ga. —, 102 S. E. 894.

Appointment by a state court of a receiver, for an insolvent corporation does not preclude a suit to foreclose a mortgage on corporate property brought in a federal court. *Brown v. Crawford*, 254 Fed. 146.

⁹² *Winsor v. Pilgrim Shoe Mach. Co.*, — R. I. —, 105 Atl. 397.

⁹³ *Welder v. Stephens Farm Loan Co.*, — Mo. —, 213 S. W. 54.

⁹⁴ *Texas Co. v. International & G. N. Ry. Co.*, 250 Fed. 742.

§ 5290. — **Contracts for personal services, including those of corporate officers.** In case of a voluntary receivership, a sales manager whose contract is thereby broken may recover the amount of prospective commissions under his contract if he is able to prove the amount lost.⁹⁵ That a corporate officer employed on contract, aided in having a receiver appointed for the corporation, or made a contract with the receiver continuing his employment, does not estop him from enforcing a claim for breach of the contract of employment.⁹⁶

§ 5291. — **Leases.** Where a receiver temporarily retains leased property, he is liable, at least, for the fair rental value not to exceed the rent reserved in the lease.⁹⁷ Where a lease is terminated by insolvency and the appointment of a receiver for the lessee corporation, the measure of damages the lessor may recover is the difference between the rent agreed upon and that received from the insolvent and from a new tenant for the balance of the term.⁹⁸

§ 5293. Right to sue corporation—General rule.⁹⁹

§ 5294. — **Liability of corporation for acts of receivers.¹** After appointment of a receiver, the corporation is not liable for his negligence,² but is liable for torts of its officers or agents.³

⁹⁵ *Primos Chemical Co. v. Fulton Steel Co.*, 266 Fed. 937.

⁹⁶ *Primos Chemical Co. v. Fulton Steel Co.*, 266 Fed. 937.

⁹⁷ *Fleming v. Noble*, 250 Fed. 733.

⁹⁸ *In re Mullings Clothing Co.*, 252 Fed. 667.

⁹⁹ Right to foreclose mortgage, see § 5286, *supra*.

Note on "Right to bring action against corporation, or prosecute pending action, as affected by the appointment of a receiver for the corporation," see 8 A. L. R. 441.

¹ Note on "Liability of corporation on cause of action for tort arising while the corporation was

in the hands of a receiver," see L. R. A. 1918 F 320, annotating *Carlson v. Mid-Continent Development Co.*, 103 Kan. 464, L. R. A. 1918 F 318, 173 Pac. 910.

² *Glover v. Insull*, 213 Ill. App. 268.

Liability of railroad company for negligence of its receiver restated, independently of state statute making the company liable where receiver appointed by state court, in *Ft. Worth & R. G. Ry. Co. v. Burleson*, — Tex. Civ. App. —, 214 S. W. 617.

³ *Cox v. Stone*, 146 La. 81, 83 So. 385.

A railroad company may be sued for damages from acts of its receivers although the order of court discharging the receivers does not require the company to pay such damages.⁴ A railroad company is liable for negligence of its receiver, where the road has been turned back with betterments, at least to the extent of the betterments; and it is immaterial that a large amount of new stock was issued and sold after the receiver was discharged.⁵ A corporation is liable on a judgment for a tort against its receiver, out of proceeds earned by the receiver and transferred by him to the corporation, without first paying binding debts of the receiver.⁶

An order entered in receivership proceedings fixing a date within which claims must be presented, is not, where there is no sale and distribution of assets, a bar to an action against the corporation, after the discharge of the receiver, for injuries resulting from the negligence of the receiver.⁷

§ 5295. — Upon whom process may be served.⁸

§ 5301. Appointment as act of bankruptcy.⁹

§ 5303. Effect on jurisdiction of public service commission.
A receiver of a railway company is a carrier.¹⁰

IV. POWERS, RIGHTS, DUTIES AND LIABILITIES OF RECEIVERS

A. In General

§ 5304. Nature of office and whom receiver represents. A receiver is not appointed solely for the benefit of creditors but also for the benefit of stockholders.¹¹ A receiver represents

⁴ Kansas City, M. & O. Ry. Co. v. Weaver, — Tex. Civ. App. —, 217 S. W. 740.

⁵ Anderson v. Chicago, R. I. & P. R. Co., — Iowa —, 175 N. W. 583.

⁶ Chicago, R. I. & P. R. Co. v. McBride, 136 Ark. 193, 206 S. W. 149.

⁷ Anderson v. Chicago, R. I. & P. R. Co., — Iowa —, 175 N. W. 583.

⁸ Appointment of receiver for railroad as affecting service of process on agent or employee in action against company, see note in 9 A. L. R. 228.

⁹ See § 5196, *supra*.

¹⁰ Rutherford v. Union Pac. R. Co., 254 Fed. 880.

¹¹ Graselli Chemical Co. v. Aetna Explosives Co., 252 Fed. 456.

creditors as well as the corporation, and may resist proceedings to enforce transactions entered into by the corporation in fraud of its creditors,¹² although, in the absence of fraud, he can assert no rights the company could not.¹³ Where all the parties are before the court, on a petition to compel a receiver to turn over certain property, the receiver has a right, on behalf of creditors, to assert that the claim is based on a fraudulent and collusive scheme.¹⁴

§ 5305. Personal profit. Purchase by a receiver of stock of the corporation in his charge is voidable but not void.¹⁵

§ 5306. Sales by receiver. A purchaser of the property of a water company at a receiver's sale acquires no higher title than the receiver acquired and is chargeable with all the obligations of the water company to furnish water.¹⁶ Where one purchases property of an insolvent corporation at a receiver's sale, sold by order of court free from the claims of creditors, he is not liable to creditors not parties to the suit but who were given the customary notice in such cases.¹⁷

B. Powers

§ 5309. General rule.¹⁸ The receiver cannot modify an order of court.¹⁹ The practice in New Jersey is to give notice to stockholders and creditors, where they are interested, before authorizing a receiver to perform certain acts.²⁰

¹² *Wirkkala v. Wirkkala Bros. Logging Co.*, 109 Wash. 137, 186 Pac. 315.

¹³ *Moore v. Boise Land & Orchard Co.*, 31 Idaho 390, 173 Pac. 117.

¹⁴ *Wirkkala v. Wirkkala Bros. Logging Co.*, 109 Wash. 137, 186 Pac. 315.

¹⁵ *Jacob v. Uncle Sam Planting & Manufacturing Co.*, 144 La. 1006, 81 So. 604.

¹⁶ *Edinburg Irrigation Co. v. Paschen*, — Tex. Civ. App. —, 223 S. W. 329.

¹⁷ *Advance-Rumely Thresher Co. v. Moss*, — Tex. Civ. App. —, 213 S. W. 690.

¹⁸ Right of receivers of corporation which paid certain of its bonds before default and before the receivership, to withdraw pro rata security as provided for in the agreement when the bonds were issued, see *Robinson v. Security Trust Co.*, — Conn. —, 108 Atl. 665.

¹⁹ *Hanson v. Chicago & L. S. R. Co.*, 167 Wis. 335, 167 N. W. 450.

²⁰ *Hitchcock v. American Pipe &*

§ 5314. Contracts. A contract by a receiver to sell coal after expiration of the receivership is not enforceable.²¹

C. Actions by

§ 5325. Power to sue at law or in equity. Where a receiver of a railroad company, appointed by a federal court, was granted leave to sue in a state court, the order may be revoked in a proper case.²²

§ 5326. Actions in federal or state courts. An action by a general receiver of an insolvent corporation, appointed by a federal court, to collect corporate assets, is ancillary to the original suit and within the jurisdiction of the federal court without regard to citizenship of the parties.²³

§ 5327. Right to sue outside of state. A chancery receiver, including one appointed under the Alabama statutes to administer the assets of an insolvent corporation under the direction of the appointing court but not vested with an estate in the property, cannot sue outside the state.²⁴ A statutory receiver, as distinguished from a mere chancery receiver, may sue in a sister state as of right.²⁵ A receiver may sue in a foreign state to recover property sold by him as receiver although without power to sue to recover a debt due the corporation.²⁶

§ 5328. Action in name of receiver or of corporation. A receiver must sue in the name of the one having the legal right.²⁷

§ 5329. Actions or proceedings which may be brought by receiver—In general. The right of a receiver to sue is not limited to

Construction Co., 89 N. J. Eq. 440, 105 Atl. 655, distinguishing practice in federal courts.

²¹ First Nat. Bank v. White Ash Coal Co., — Iowa —, 176 N. W. 287.

²² Investment Registry v. Chicago & M. Elec. R. Co., 251 Fed. 510.

²³ Hume v. City of New York, 255 Fed. 488.

²⁴ Sterrett v. Second Nat. Bank,

248 U. S. 73, 63 L. Ed. 135, aff'g 246 Fed. 753.

²⁵ Hopkins v. Lancaster, 254 Fed. 190.

²⁶ Chicago Bonding & Surety Co. v. United States ex rel. Frank Adams Elec. Co., 261 Fed. 266.

²⁷ State ex rel. Elberta Peach & Land Co. v. Chicago Bonding & Surety Co., 279 Mo. 535, 215 S. W. 20.

cases where the corporation could have sued,²⁸ although it has been held that a receiver cannot recover on a cause of action personal to creditors and one which would not have vested in the corporation.²⁹

§ 5332. — Actions against corporate officers.³⁰

§ 5337. Parties to actions by receivers. A receiver should be joined as a plaintiff in an action by a stockholder to enjoin a sale of corporate property under a deed of trust pending an action for dissolution and a receiver.³¹

D. Duties, Liabilities and Actions Against

§ 5338. Right to sue receiver. A judgment cannot be entered against a receiver and the corporation in the same suit.³²

§ 5342. Liabilities—Liability for torts of employees. It is no defense to a tort action against a receiver that the damages will in reality be imposed upon innocent creditors and stockholders.³³ A receiver may be held liable for exemplary damages for the wilful, oppressive or malicious acts of his employees.³⁴ A receiver of a corporation is not liable as the "owner, keeper or harbinger" of a dog belonging to an employee of the company where he had no knowledge that the dog was on the premises.³⁵

§ 5345. Defense of statute of limitations. The appointment of a receiver does not stop the running of the statute of limitations;³⁶ and this applies to limitations against the claim of a creditor of an insolvent bank.³⁷

²⁸ Drennen v. Southern States Fire Ins. Co., 252 Fed. 776, 787.

²⁹ Fordham v. Poor, 109 N. Y. Misc. 187, 179 N. Y. Supp. 367.

³⁰ See § 2676, supra.

³¹ Lasley v. Scales, 179 N. C. 578, 103 S. E. 214.

³² Belke v. Bush, 213 Ill. App. 29.

³³ Cox v. Stone, 146 La. 81, 83 So. 385.

³⁴ Gardner v. Martin, — Miss. —, 85 So. 182.

³⁵ Markwood v. McBroom, — Wash. —, 188 Pac. 521.

³⁶ Houston Oil Co. v. Brown, — Tex. Civ. App. —, 202 S. W. 102. See also Interurban Const. Co. v. Central State Bank, 76 Okla. 281, 184 Pac. 905.

³⁷ England v. Hughes, 141 Ark. 235, 217 S. W. 13.

§ 5347. **Statutes imposing penalties or liabilities on corporations as applicable to receivers.** The New York statute imposing penalties on "any railroad corporation" for receiving fares in excess of the lawful rate, does not apply to receivers.³⁸ However, a receiver of a railroad appointed by a federal court must operate it according to the valid laws of the state where located.³⁹ A presumption of negligence arising from stated facts as against a railroad company also arises against a receiver when he is operating a road.⁴⁰

§ 5348. **Service of summons in actions against receivers.** Where receivers of a railroad company are sued, process may be served on any person who is competent to receive service in an action against the railroad company.⁴¹

V. RECEIVER'S CERTIFICATE

§ 5350. **Power to issue—General rules.** In case of public service companies, receiver's certificates may be authorized, in order to run the business.⁴² It is within the discretion of the court whether to permit a railroad receiver to issue receiver's certificates constituting a lien prior to an existing mortgage.⁴³

§ 5351. — **In case of strictly private corporations.** In case of purely private corporations, receivers' certificates with a prior lien over all other claims should not be issued to complete improvements.⁴⁴

§ 5352. **Purposes for which permissible.** In case of a small branch railroad, which does not pay the cost of operation, residents cannot require continued operation by issuance of receivers' certificates, where all the stockholders and creditors object, unless such residents give security for any loss occasioned by continued operation.⁴⁵

³⁸ Merksamer v. Garrison, 111 N. Y. Misc. 195, 181 N. Y. Supp. 197.

³⁹ Westinghouse Elec. & Mfg. Co. v. Binghamton Ry. Co., 255 Fed. 378.

⁴⁰ Lamb v. Floyd, 148 Ga. 357, 1 A. L. R. 1172 with note, 96 S. E. 877.

⁴¹ Chicago, R. I. & P. R. Co. v. Owens, 78 Okla. 114, 189 Pac. 171.

⁴² Central Bank & Trust Corporation v. Cleveland, 252 Fed. 530.

⁴³ Central Trust Co. v. Pittsburgh, S. & N. R. Co., — N. Y. —, 128 N. E. 114.

⁴⁴ Pittsburgh Plate Glass Co. v. Huberty, 213 Ill. App. 315.

⁴⁵ Central Bank & Trust Corporation v. Cleveland, 252 Fed. 530.

§ 5354. **Validity.** The estoppel of bondholders to attack receivers' certificates extends to their transferees.⁴⁶

§ 5358. **Priorities.** Where all the other bondholders consented to receivers' certificates to be made a lien prior to the mortgage, the nonconsenting bondholder is not entitled to priority where he raised no objections to the issuance of certificates, etc.⁴⁷ Mortgage bonds of a holding company owning street railway stock but not operating any lines at the time should not be subordinated to receiver's certificates thereafter issued where only a little of their proceeds was expended on mortgaged property.⁴⁸

VI. PRESENTATION AND PAYMENT OF CLAIMS AND DISTRIBUTION OF FUNDS

A. General Rules

§ 5366. **Presentation and proof—Mode of presenting and proving.**⁴⁹ The production of a note admitted to be the note of the corporation is sufficient in the absence of any defense by the receiver.⁵⁰

§ 5367. — **Objections by creditors.** It is no ground for an objection to the allowance of claims of creditors against an insolvent company in the hands of a receiver that the particular creditor was not entitled to share in a specified fund.⁵¹

§ 5368. **What claims are provable—General rules.**⁵² The fact that a claim was not liquidated when the receiver was appointed is no objection to its allowance.⁵³ The possessor of a matured

⁴⁶ Pillinger v. Beaty, 265 Fed. 551.

⁴⁷ Lake v. Mudgett, 252 Fed. 365.

⁴⁸ Westinghouse Elec. & Mfg. Co. v. Brooklyn Rapid Transit Co., 260 Fed. 550.

⁴⁹ Procedure as to filing claims, see Independent Van & Storage Co. v. Iowa Mercantile Co., — Iowa —, 179 N. W. 157.

⁵⁰ General Elec. Co. v. Interstate

Elec. Co., — Mo. App. —, 204 S. W. 933.

⁵¹ Standard Lithographing & Printing Co. v. Twin City Motor Speedway Co., 139 Minn. 120, 165 N. W. 967.

⁵² Claims provable in receivership proceedings, see article in 28 L. J. 673-680.

⁵³ National Roofing Tile Co. v. McDonald, — Conn. —, 108 Atl. 726.

claim enforceable in the state where the contract out of which it grew was to be performed, should be allowed his claim although not enforceable by action under the rules of practice and procedure in the state where the receiver was appointed.⁵⁴

§ 5369. — Services of attorneys. The corporation should bear the expense of legal services incurred by a stockholder in intervening in a receivership in a federal court outside the state, where the intervention was warranted.⁵⁵

§ 5370. — Taxes in general. The liability for taxes is not affected by a receivership.⁵⁶ While the authorities are in conflict, the rule in the federal courts is that taxes should be paid by a receiver, where the corporation would have been liable to pay taxes accruing during the receivership.⁵⁷ Where a receiver continues operation of a street railway, franchise taxes should be paid by him.⁵⁸ The claim of the state for a license tax imposed on foreign corporations for the privilege of doing business in the state is a tax entitled to priority in receivership proceedings in New York.⁵⁹

§ 5373. Compensation of receiver.⁶⁰ A statute fixing compensation of receivers ordinarily will not be construed as retrospective.⁶¹ If a receivership is improperly granted, all costs, including the salary of the receiver, are taxable against the person procuring the receivership.⁶²

§ 5374. As of what time status and amount of claims fixed. The general rule is that the status of creditors of an insolvent corporation is fixed as of the date of the order of dissolution, or of the appointment of a receiver, and not that of filing the bill.⁶³

⁵⁴ National Roofing Tile Co. v. McDonald, — Conn. —, 108 Atl. 726.

⁵⁵ Hitchcock v. American Pipe & Construction Co., 89 N. J. Eq. 440, 105 Atl. 655.

⁵⁶ Union Trust Co. v. Great Eastern Lumber Co., 248 Fed. 46.

⁵⁷ Bright v. Arkansas, 249 Fed. 950.

⁵⁸ Harvey v. Bay State St. R. Co., — Mass. —, 125 N. E. 614.

⁵⁹ Sweet v. All Package Grocery Stores Co., 262 Fed. 727.

⁶⁰ Rules governing compensation of receiver, see Clifford v. Montgomery, 202 Ala. 609, 81 So. 551.

⁶¹ State v. State Bank & Trust Co., 43 Nev. 388, 187 Pac. 1002.

⁶² Hook v. Payne, — Tex. Civ. App. —, 211 S. W. 280.

⁶³ O'Neil v. Burnett, 263 Pa. 216, 106 Atl. 246.

§ 5377. Interest on claims. Interest on debts of an insolvent corporation in the hands of a receiver will be calculated only to the date of his appointment.⁶⁴ Interest on claims against an insolvent estate, whether allowable as matter of contract or as matter of damages, but certainly where allowable only as matter of damages, ceases to run upon the property being taken in custodia legis, and this rule applies as well to preferred as to general claims; but this rule is subject to exceptions.⁶⁵ Where property subject to a mortgage foreclosure decree is sold by a statutory receiver in insolvency proceedings, free from the lien, the lien attaches to the proceeds, and where the proceeds are more than sufficient to pay the decree with interest, interest should be allowed to the date of the payment of the purchase price to the receiver, and after that date interest should be allowed only so far as actually earned by the portion of the purchase price upon which the lien attached.⁶⁶

B. Priorities

§ 5380. In general. Funds derived from operation by a receiver, in excess of expenses, are distributable among creditors according to their rank and priority, determinable in the same manner as if execution at law had been levied.⁶⁷ A guarantor of a debt of a corporation afterwards going into the hands of a receiver is not entitled to priority, on the doctrine of subrogation, where it had paid only part of the debt for which it was liable.⁶⁸ The state is not entitled to preference over other creditors.⁶⁹

A judgment against a receiver establishing the priority of a claim against the insolvent corporation is res judicata in any subsequent proceeding involving priority of claims.⁷⁰

⁶⁴ New York Trust Co. v. Detroit, T. & I. R. Co., 251 Fed. 514.

⁶⁵ Hoover Steel Ball Co. v. Schaefer Ball Bearing Co., 90 N. J. Eq. 515, 107 Atl. 425.

⁶⁶ Hoover Steel Ball Co. v. Schaefer Ball Bearing Co., 90 N. J. Eq. 515, 107 Atl. 425.

⁶⁷ Pennsylvania Co. for Insurance v. Philadelphia Co., 266 Fed. 1.

⁶⁸ Pennsylvania Co. for Insurance v. Philadelphia Co., 266 Fed. 1.

⁶⁹ Aetna Casualty & Surety Co. v. Moore, 107 Wash. 99, 181 Pac. 40.

⁷⁰ State ex rel. Crittenberger v. Farmers' & Merchants' Bank, — Ind. App. —, 124 N. E. 501.

§ 5381. Income of receivership as subject to mortgage. A receiver is entitled to the profits of a mine as against the mortgagee, under the Arizona statutes, where the mortgagee is not in possession and has not foreclosed.⁷¹ Where a receiver is in possession of mortgaged property, the remedy of the mortgagee is to apply for an order extending the receivership for his benefit, in order to secure rents from such property.⁷²

§ 5392. Trust funds. Trust property or its proceeds may be followed into the hands of a receiver.⁷³ Money due a bridge company by a railroad company, for use of the bridge, is not a trust fund so as to be entitled to priority.⁷⁴

§ 5393. Statutory priorities—In general.⁷⁵ Statutory priority of a landlord's lien on personal property includes only tangible personal property.⁷⁶

§ 5394. — Claims of laborers. A person is not a "clerk or servant" entitled to preference where he works away from the place of business, is not employed exclusively by the corporation, is only bound to do a particular class of work, and is not working under the control or subject to the commands of the corporation.⁷⁷

"Preference of wages over lien creditors of corporation in hands of receiver, in absence of statutory provision therefor" is the subject of a recent extensive annotation.⁷⁸

§ 5396. Expenses of receivership, including operation of business, after appointment of receiver. The lessor of a theater to an amusement company which went into the hands of a receiver

⁷¹ London-Arizona Consol. Copper Co. v. Gila Copper Sulphide Co., 257 Fed. 324.

⁷² London-Arizona Consol. Copper Co. v. Gila Copper Sulphide Co., 257 Fed. 324.

⁷³ Farnsworth v. Muscatine Produce & Pure Ice Co., 177 Iowa 21, 158 N. W. 741.

⁷⁴ Louisville Bridge Co. v. Chicago, I. & L. Ry. Co., 253 Fed. 631.

⁷⁵ See also §§ 1435-1437, supra.

⁷⁶ Louisville Gayety Theatre Co. v. Ragan, 186 Ky. 672, 217 S. W. 929.

⁷⁷ In re Ashley & Smith, Ltd., [1918] 2 Ch. Div. 378.

⁷⁸ 5 A. L. R. 690, annotating Florida Construction & Realty Co. v. Pournell, 76 Fla. 395, 5 A. L. R. 685, 80 So. 54.

is not entitled to priority for rent over other operating expenses of the theater.⁷⁹

§ 5399. Expenses of operation of business before appointment of receiver—General rule.⁸⁰ Operating expenses, under the New Jersey statute, are entitled to priority over a vendor's lien.⁸¹ The six months' rule applies only to surplus income in the hands of the receiver after paying all operating expenses and taxes.⁸² The seller of coal to a corporation, delivery being made on the day a receiver was appointed, has no preferred claim unless (1) the corporation was insolvent at the time of the purchase, (2) it concealed its insolvency, and (3) it purchased the coal without the intention of paying for it.⁸³

Interest on six months' claims, although running to the appointment of a receiver, does not run after that date, where the proceeds of sale are insufficient to pay any part of the mortgage debt and there is no diversion of income.⁸⁴ The six months' rule as to supplies furnished prior to the receivership properly includes interest to the time of payment, even though the corporation is insolvent.⁸⁵

§ 5401. — Rule as limited to railroad or to quasi public corporations. Costs of receivership are entitled to priority over all liens, including vendor's liens, in case of quasi public service companies such as cemetery associations.⁸⁶

⁷⁹ Louisville Gayety Theatre Co. v. Ragan, 186 Ky. 672, 217 S. W. 929.

⁸⁰ Six months' rule in general, see New York Trust Co. v. Detroit, T. & I. R. Co., 251 Fed. 514; Baltimore Trust Co. v. Western U. Tel. Co., 149 Ga. 262, 99 S. E. 868; Baltimore Trust Co. v. Seaboard Air-Line R. Co., 149 Ga. 260, 99 S. E. 867; Interurban Const. Co. v. Central State Bank, 76 Okla. 281, 184 Pac. 905.

Mortgagee's claim for coal mined before the receivership in depletion of the security, held a general and not a preferred claim

in Goodman Mfg. Co. v. Pittsburgh-Buffalo Co., 265 Fed. 561.

⁸¹ Bliss v. Linden Cemetery Ass'n, — N. J. L. —, 109 Atl. 500.

⁸² Interurban Const. Co. v. Central State Bank, 76 Okla. 281, 184 Pac. 905.

⁸³ Hyman v. Trow Directory Printing & Bookbinding Co., 261 Fed. 991.

⁸⁴ New York Trust Co. v. Detroit, T. & I. R. Co., 251 Fed. 514.

⁸⁵ Texas Co. v. International & G. N. Ry. Co., 250 Fed. 742.

⁸⁶ Bliss v. Linden Cemetery Ass'n, 90 N. J. Eq. 404, 107 Atl. 594.

§ 5402. — **Rule as affected by diversion of income.** Six months' preferences apply only when there has been a diversion of income.⁸⁷

§ 5403. — **Claims entitled to priority within rule.** Supply creditors are entitled to priority over bondholders.⁸⁸ Where credit is extended on the strength of the railroad company's general credit, in case of claims for use of a bridge by the railroad under a contract giving the bridge company the right to terminate it at any time for nonpayment of amounts due, the debt is not one for "current expenses" so as to be entitled to priority.⁸⁹

§ 5404. — **Length of time to which priority extends back.** In determining whether six months is to be deemed the limit for priorities of current expenses, the fact that the claim arose under a contract providing for its termination in case of default for thirty days, is material.⁹⁰

⁸⁷ First Trust Co. v. Illinois Cent. R. Co., 252 Fed. 965.

⁸⁸ See Mayotown Lumber Co. v. Nacogdoches Grocery Co., — Tex. Civ. App. —, 221 S. W. 644.

⁸⁹ Louisville Bridge Co. v. Chicago, I. & L. Ry. Co., 253 Fed. 631.

⁹⁰ Louisville Bridge Co. v. Chicago, I. & L. Ry. Co., 253 Fed. 631.

CHAPTER 64

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¹See *Subsidiary High Court of tarino*, — Cal. App. —, 183 Pac. Ancient Order of Foresters v. Pes- 297.

§ 5409. Methods of dissolution—As affected by nature of corporation.²

§ 5411. Right to urge forfeiture or dissolution in collateral proceeding. Alleged fraud in the method of creating a corporation cannot be urged in a collateral proceeding to which neither the corporation nor its incorporators are parties.³

III. BY EXPIRATION OF TIME

§ 5417. General rules. Unless corporate existence is continued in the manner fixed by law, corporate life expires ipso facto and without any direct action at the time fixed by the charter for expiration.⁴

§ 5422. Extension or shortening of corporate existence. A corporation has power to shorten the term of its corporate existence by amending its articles of incorporation, even if the practical result of such amendment is almost an immediate dissolution.⁵

§ 5424. Effect of lapse of time. A corporation is dissolved at the expiration of the term of its corporate existence.⁶

IV. BY ACTS OR OMISSIONS OPERATING AS DISSOLUTION WITHOUT RECOURSE TO THE COURTS

§ 5425. Ipso facto dissolution—General rule. Constitutional or statutory provisions will not be construed as providing for a dissolution ipso facto except in clear cases.⁷

§ 5426. — Acts required or prohibited by charter or statute where acts not expressly stated to be, of themselves, a dissolution. The fact that a corporation incorporated by a special

² Note on "Dissolution or termination of existence of religious society," see Ann. Cas. 1918 D 1056.

³ Randle v. Walker, — Ala. App. —, 84 So. 551.

⁴ Rossing v. State Bank, 181 Iowa 1013, 165 N. W. 254.

⁵ Nezik v. Cole, — Cal. App. —, 184 Pac. 523.

⁶ Nezik v. Cole, — Cal. App. —, 184 Pac. 523.

⁷ Elliott's Knob Iron, Steel & Coal Co. v. State Corporation Commission, 123 Va. 63, 96 S. E. 353.

act has not engaged in business in the state and has failed to comply with statutory provisions relating to acceptance of the state constitution, filing the name of an agent on whom process may be served, etc., does not ipso facto dissolve the corporation.⁸

§ 5429. Failure of railroad company to commence or finish construction of road within specified time. A charter is not ipso facto forfeited by failure of the company to comply with a condition subsequent, such as completion of construction within five years.⁹

§ 5433. Failure or loss of an integral part—Resignation, removal or death of officers. A corporation is not dissolved by lack of officers.¹⁰

§ 5436. Suspension of business or nonuser of franchises. Cessation of business does not ipso facto dissolve a corporation.¹¹

§ 5443. Failure to pay taxes or license fees.¹² Failure to pay taxes does not ordinarily ipso facto dissolve the corporation.¹³ The 1917 California Corporate License Act providing that, for failure to pay a license tax, the corporate rights and powers shall be suspended, with certain exceptions, does not require a proclamation of the governor to make the suspension effective, and no decree need be entered in a sister state to make the sus-

⁸ Reichert v. Ellis Ferry Co., 184 Ky. 150, 211 S. W. 403.

⁹ People v. Hudson River Connecting R. Corporation, 228 N. Y. 203, 126 N. E. 801.

¹⁰ Jones Min. Co. v. Cardiff Mining & Milling Co., — Utah —, 191 Pac. 426.

¹¹ Jones Min. Co. v. Cardiff Mining & Milling Co., — Utah —, 191 Pac. 426.

¹² Evidence of proclamation of governor dissolving corporation for failure to pay license fees as raising a presumption that he acted on a report from the corporation commissioner, see Smyth v.

Kenwood Land Co., — Ore. —, 190 Pac. 962.

Time within which corporation may be reinstated, under North Dakota statutes, where charter has been canceled by state for failure to file annual reports and pay fees, and procedure, see Missouri Slope Agricultural & Fair Ass'n v. Hall, — N. D. —, 177 N. W. 369.

¹³ Elliott's Knob Iron, Steel & Coal Co. v. State Corporation Commission, 123 Va. 63, 96 S. E. 353, holding regular assessment of fee by commission, etc., condition precedent to revocation of charter.

pension operative there.¹⁴ Under the 1915 California statute, as distinguished from the 1905 statute, the dissolution of a corporation, for failure to pay license and franchise tax, dates from the nonpayment rather than from the proclamation of the governor.¹⁵ In Texas, failure to pay the annual license tax does not ipso facto forfeit the charter.¹⁶ The Virginia Constitution and statutes do not make the failure to pay registration fee and taxes operate of itself as a forfeiture of the charter.¹⁷

V. VOLUNTARY DISSOLUTION

§ 5447. Power in general. A stockholder cannot enjoin the doing of the legal act of assessing capital stock to pay debts and disincorporating in order to incorporate in another state.¹⁸ A public service corporation may voluntarily dissolve where its business cannot be operated except at a loss.¹⁹

§ 5448. Transfer of property and franchises under legislative authority. A corporation is dissolved by a trust agreement signed by all the stockholders whereby the trustees are to turn over all the assets for stock in a new company to be formed.²⁰

§ 5451. Who may dissolve or surrender charter independently of statute. Dissolution of a trust company by a corporation owning stock therein is not ultra vires even though the corporation acted beyond its authority in creating the trust company.²¹

§ 5457. Statutory regulations—Grounds for granting or refusing dissolution.²² A voluntary dissolution is properly or-

¹⁴ *Siegel v. Maryland Casualty Co.*, 178 N. Y. Supp. 391.

¹⁵ *California Nat. Supply Co. v. Flack*, — Cal. —, 190 Pac. 634.

¹⁶ *Bunn v. City of Laredo*, — Tex. Civ. App. —, 213 S. W. 320.

¹⁷ *Elliott's Knob Iron, Steel & Coal Co. v. State Corporation Commission*, 123 Va. 63, 96 S. E. 353.

¹⁸ *Dammann v. Hydraulic Clutch Co.*, — Cal. App. —, 187 Pac. 1069.

¹⁹ *Moore v. Lewisburg & R. E.*

R. Co., 80 W. Va. 653, L. R. A. 1918 A 1028, 93 S. E. 762.

²⁰ *Irons v. Croft Hat & Notion Co.*, — W. Va. —, 104 S. E. 111.

²¹ *Holmes v. Crane*, 191 N. Y. App. Div. 820, 182 N. Y. Supp. 270.

²² The decision in *Allen v. Distilling Co. of America*, 87 N. J. Eq. 531, 100 Atl. 620, as set forth on page 9074 in vol. 8 is affirmed under the title of *United States Industrial Alcohol Co. v. Distill-*

dered, in New York, where the stock is owned by two who cannot agree.²³ The provision of the New York statute as to dissolution where a corporation "has an even number of trustees or directors" does not apply, it seems, to corporations happening to have an even number of directors at a particular time by reason of some vacancies on the board.²⁴ In New York, under § 170 of the General Incorporation Law, an application by a majority of the directors for dissolution should not be granted although the company is insolvent, where some stockholders desire to sue to cancel a lease and for neglect of duty by directors; and it is proper to give leave to renew the petition in three months if no such action is brought in the meantime.²⁵ Under the New York statute authorizing a voluntary dissolution of a corporation on the adoption of a resolution by the directors that it is, in their opinion, advisable, where approved by two-thirds of the stock at a stockholders' meeting, the directors must act in good faith and cannot consider their personal wishes or advantage or the antagonism between themselves and other stockholders.²⁶ The expediency of a voluntary dissolution will not be reviewed by the courts; but relief will be granted minority stockholders where the dissolution is the result of bad faith or other breach of trust on the part of the directors or managing stockholders.²⁷

The discretion of majority stockholders to dissolve the corporation will not be interfered with by the courts although the company is not insolvent nor because the ground is merely a doubt as to future business.²⁸

ing Co. of America, 89 N. J. Eq. 177, 104 Atl. 216.

²³ Application of Bown Bros., Inc., 111 N. Y. Misc. 294, 181 N. Y. Supp. 460.

²⁴ In re Friedlieb, 184 N. Y. Supp. 753.

²⁵ In re Quicksilver Min. Co., 186 N. Y. App. Div. 347, 174 N. Y. Supp. 338.

²⁶ Directors are not authorized to dissolve a corporation, under the New York statutes, where they act "in bad faith, fraudulently, or through the intent to punish or

oppress a stockholder because he defends himself in the courts or otherwise against their illegal and unfair acts relative to the corporation or because of any other reason." *Kavanaugh v. Kavanaugh Knitting Co.*, 226 N. Y. 185, 123 N. E. 148, rev'g 184 N. Y. App. Div. 650, 172 N. Y. Supp. 576.

²⁷ *Kavanaugh v. Kavanaugh Knitting Co.*, 226 N. Y. 185, 123 N. E. 148, rev'g 184 N. Y. App. Div. 650, 172 N. Y. Supp. 576.

²⁸ *Rossing v. State Bank*, 181 Iowa 1013, 165 N. W. 254.

A petition for voluntary dissolution should be denied where it states that all the directors are in favor of a dissolution when in fact one of the three was not in favor of it at the time of the filing of the petition.²⁹

§ 5458. — Effect of motives of majority stockholders and rights of minority stockholders. Statutes authorizing a voluntary dissolution contemplate a dissolution in fact as well as in name, and should not be allowed where merely a scheme of the majority stockholders to turn the property over to another corporation.³⁰ Where the statute authorizing a voluntary dissolution requires that the act of the directors be ratified by two-thirds of the stock, and the directors voting for dissolution owned two-thirds of the stock, they, as majority stockholders, occupy a relation of trust, and they cannot, in voting to ratify the dissolution, use their controlling power in bad faith or for their individual advantage or purpose.³¹ The Missouri statute authorizing a dissolution of a corporation where two-thirds of the stock consent thereto does not permit majority stockholders of a prosperous corporation to dissolve it in order to effect a consolidation with another company, and thereby compel dissenting stockholders to take stock in a new company or accept the price fixed by them to be paid for the stock of the dissenters.³²

§ 5459. — Who may apply for dissolution. A holder of the majority of the stock of a corporation cannot sue for a dissolution, under section 171 of the New York General Corporation Law, without first petitioning the directors to petition for a dissolution as provided for therein.³³

§ 5463. — Procedure to accomplish dissolution.³⁴

²⁹ *In re Cowles Realty Co.*, 193 N. Y. App. Div. 874, 184 N. Y. Supp. 778.

³⁰ *In re Doe Run Lead Co.*, — Mo. —, 223 S. W. 600.

³¹ *Kavanaugh v. Kavanaugh Knitting Co.*, 226 N. Y. 185, 123 N. E. 148, rev'g 184 N. Y. App. Div. 650, 172 N. Y. Supp. 576.

³² *In re Doe Run Lead Co.*, — Mo. —, 223 S. W. 600.

³³ *In re Friedlieb*, 184 N. Y. Supp. 753.

³⁴ Dissolution proceedings by corporation as proceedings in equity, and right to appeal, see *In re Doe Run Lead Co.*, — Mo. —, 223 S. W. 600.

VI. INVOLUNTARY DISSOLUTION BY DECREE OF COURT

A. General Considerations

§ 5471. Governing principles in action by state—Necessity that nonuser or misuser be wilful. To warrant dissolution, for neglect or refusal to perform charter duties, a bad or corrupt motive is not necessary.³⁵

B. Grounds for Forfeiture

§ 5482. Misuser or abuse of franchises or powers—General rule.³⁶ Abuse of the franchise, i. e., misuser is ground for forfeiture of the charter although the same acts may constitute a violation of a penal statute.³⁷

§ 5483. — Ultra vires acts. A corporation will not be dissolved because of unlawfully practicing dentistry where the legislature has cured the want of such power before the commencement of the action to dissolve.³⁸

§ 5499. Breach of conditions subsequent prescribed by charter or other statute—Failure to file annual report or other papers. The charter of a domestic corporation which transacts all its business outside the state may be forfeited by a court for failure to file annual reports, etc., as required by statute, as well as the charter of the domestic corporations doing business in the state, under the South Dakota statutes.³⁹ Failure to file a certificate showing that half of the capital stock was paid in within a year after incorporation, as required by the New York

³⁵ State ex rel. Chamberlain v. Public Drug Co., 41 S. D. 287, 170 N. W. 161.

³⁶ "Abuse of its powers," meaning of as used in statute enumerating as one of the grounds for forfeiture of charter, the violation of "the provisions of any law by which such corporation shall have forfeited its corporate rights, privileges and franchises by abuse of its power," see State

ex rel. Langer v. Gamble-Robinson Fruit Co., — N. D. —, 176 N. W. 103.

³⁷ State ex rel. Langer v. Gamble-Robinson Fruit Co., — N. D. —, 176 N. W. 103.

³⁸ Lewis v. Woodbury Dental Parlors Co., 106 N. Y. Misc. 78, 175 N. Y. Supp. 269.

³⁹ State ex rel. Chamberlain v. Public Drug Co., 41 S. D. 287, 170 N. W. 161.

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Business Corporations Law, is not ground for an action to vacate a charter where the annual report of the corporation has been filed and the taxes paid on the stock.⁴⁰

§ 5504. Nonuser as ground—As statutory ground.⁴¹

§ 5510. Suspension or abandonment of business—As statutory ground.⁴² A temporary deficiency of cash needed for operating expenses, is not a "lack of funds," within a statute authorizing dissolution where a corporation "shall suspend its ordinary business for the lack of funds to carry" it on, where the corporate assets are amply sufficient to supply a basis for needed financing.⁴³ In North Carolina, by statute, a minority stockholder may obtain a dissolution of the corporation where it has not attempted to carry on business for more than two years.⁴⁴

§ 5518. Fraud, illegality of purpose of corporation, etc. Organizing a \$2,000 corporation and immediately increasing its capital stock to \$150,000, to evade a statute as to the amount of capital stock necessary to commence business, is a fraud on the law warranting the cancellation of the charter.⁴⁵

D. Jurisdiction, Who May Sue, and Procedure in Actions by State

§ 5531. Jurisdiction of courts—Jurisdiction over foreign corporations.⁴⁶

§ 5532. Who may sue. In Texas quo warranto cannot be brought to forfeit a charter by a district or county attorney but only by the attorney general.⁴⁷

⁴⁰ *In re Lewis*, 189 N. Y. App. Div. 359, 178 N. Y. Supp. 533.

⁴¹ See § 5510, *infra*.

⁴² When corporation "ceases" to do business, within the Illinois statute, so as to be subject to dissolution at the suit of creditors, see *Baker v. Abbott Mfg. Co.*, 212 Ill. App. 476, 479.

⁴³ *Miller v. Herzberg*, 202 Ala. 613, 81 So. 555.

⁴⁴ *Lasley v. Walnut Cove Mercantile Co.*, 179 N. C. 575, 103 S. E. 213.

⁴⁵ *Randle v. Walker*, — Ala. App. —, 84 So. 551.

⁴⁶ See § 5703, *infra*.

⁴⁷ *State ex rel. Francis v. Wal-ler*, — Tex. Civ. App. —, 211 S. W. 322.

§ 5534. Proceedings to obtain forfeiture and decree—Parties. It is not necessary that officers and directors be joined as parties to an action to forfeit a corporate charter for failure to comply with statutory provisions.⁴⁸

§ 5535. — Venue. An action to forfeit a charter, for failure to obey statutes, brought by the state's attorney, may be commenced, under the South Dakota statutes, in any county of the state, on leave of court.⁴⁹

§ 5536. — Pleading.⁵⁰

§ 5539. — Decree. Instead of dissolving the corporation, the court, in a quo warranto proceeding, will declare a partial ouster where the public as well as innocent owners would sustain severe losses from a dissolution.⁵¹ A stockholder who stands by with full knowledge of steps being taken to dissolve the corporation is not estopped to thereafter object to the dissolution, where no injury has resulted.⁵²

F. Actions by Minority Stockholders to Obtain Dissolution

§ 5543. General rule.⁵³ The rights of a minority stockholder to a dissolution is to be determined according to the conditions as of the date of the filing of the bill.⁵⁴

§ 5546. Exceptions to rule—Difference of opinion. Minority stockholders cannot have a corporation dissolved merely because they are not satisfied with the way the majority is conducting

⁴⁸ State ex rel. Chamberlain v. Public Drug Co., 41 S. D. 287, 170 N. W. 161.

⁴⁹ State ex rel. Chamberlain v. Public Drug Co., 41 S. D. 287, 170 N. W. 161.

⁵⁰ Sufficiency of bill in the nature of a quo warranto to dissolve corporation, for violation of contract, see Eutaw Ice, Water & Power Co. v. City of Eutaw, 202 Ala. 143, 79 So. 609.

⁵¹ State ex rel. Attorney General v. Combination Oil & Gas Co., 105 Kan. 340, 182 Pac. 547.

⁵² In re Doe Run Lead Co., — Mo. —, 223 S. W. 600.

⁵³ Note on "Right of minority stockholder or stockholders to maintain suit to wind up or dissolve corporation," see Ann. Cas. 1918 E 424.

⁵⁴ Dixie Lumber Co. v. Hellams, 202 Ala. 488, 80 So. 872.

the corporation, where the majority are acting in good faith and exercising their best judgment.⁵⁵

§ 5547. — **Exception where purpose of corporation is impossible of attainment.** In Alabama, a corporation will not be dissolved at the suit of a minority stockholder merely because for several years it has operated at a loss, where the corporation is solvent and a going concern, and it is not shown to a moral certainty that continuation of business will result in serious loss in the near future.⁵⁶ Whether the corporation's purpose is one impossible of execution, so that it may be terminated at the complaint of any stockholder, is not a matter to be determined by the weight of evidence, but instead "it must be a certainty, as things are deemed to be certain in law."⁵⁷ Objects of a corporation have failed "only when their pursuit has been completely abandoned, or their attainment has become impossible."⁵⁸ A land company will not be dissolved at the suit of minority stockholders on the theory that further pursuit of the scheme is impossible because of lack of available cash, where there are no debts and the assets supply an ample basis of credit for financing future operations.⁵⁹ The fact that a land company expected to sell most of its lots before the boom ended, but failed to do so, does not show "a failure of the object of the corporation," within the Alabama statute, so as to entitle minority stockholders to a dissolution.⁶⁰

§ 5548. — **Exception in case of fraud or mismanagement.**⁶¹

§ 5549. — **Exception where corporation not a going concern.** Suspension of street improvements and selling of lots during the period of industrial depression following the world war, by a land company, is not an abandonment of the business, within

⁵⁵ *Beeler v. Standard Inv. Co.*, 107 Wash. 442, 5 A. L. R. 363, 181 Pac. 896.

⁵⁶ *Dixie Lumber Co. v. Hellams*, 202 Ala. 488, 80 So. 872.

⁵⁷ *Miller v. Herzberg*, 202 Ala. 613, 81 So. 555, quoting *Phinizy v. Anniston City Land Co.*, 195 Ala. 656, 71 So. 469.

⁵⁸ *Miller v. Herzberg*, 202 Ala. 613, 81 So. 555.

⁵⁹ *Miller v. Herzberg*, 202 Ala. 613, 81 So. 555.

⁶⁰ *Miller v. Herzberg*, 202 Ala. 613, 81 So. 555.

⁶¹ This section is quoted in *Bordages v. Burnett*, — Tex. Civ. App. —, 221 S. W. 326.

the Alabama statute, so as to entitle minority stockholders to a dissolution.⁶²

§ 5551. Statutory authority to sue—Grounds as enumerated by statute. The 1913 North Carolina statute providing for dissolution on application of stockholders owning at least one-fifth of the stock has no application to actions to dissolve for nonuser of corporate powers.⁶³ The voluntary sale of corporate assets and failure to distribute the proceeds among the stockholders, abandonment of the business, and failure to hold any stockholders' or directors' meetings for two years, is ground for dissolution in a suit by one-fifth of the stockholders, under the West Virginia statute authorizing dissolution in such an action where "sufficient cause" is shown.⁶⁴

§ 5554. Conditions precedent—Demand on officers or majority stockholders to correct evil. Application to the directors to act is not a condition precedent to an action by minority stockholders for dissolution because of nonuser of corporate powers for over two years.⁶⁵

§ 5561. Procedure, parties, pleading, etc. Where a court has obtained jurisdiction of an action to dissolve a corporation, it may sell the property through its own appointees, without regarding minor requirements of deeds of trust, where such a course works no substantial impairment of the value of the security.⁶⁶

G. Actions by Creditors to Obtain Dissolution

§ 5562. General rule. The pendency of a suit by an unsecured creditor or stockholder to wind up the business and administer the assets of an insolvent corporation does not bar

⁶² *Miller v. Herzberg*, 202 Ala. 613, 81 So. 555.

⁶³ *Lasley v. Walnut Cove Mercantile Co.*, 179 N. C. 575, 103 S. E. 213.

⁶⁴ *Williams v. Croft Hat & Notion Co.*, 82 W. Va. 549, 96 S. E. 929.

⁶⁵ *Lasley v. Walnut Cove Mercantile Co.*, 179 N. C. 575, 103 S. E. 213.

⁶⁶ *Lasley v. Seales*, 179 N. C. 578, 103 S. E. 214.

the right of a pledgee of corporate bonds, the corporation being the pledgor, to sell the bonds after default.⁶⁷

VII. EFFECT OF DISSOLUTION

§ 5567. Extraterritorial effect of dissolution. A suspension of corporate rights, under the 1917 California statute, for failure to pay taxes, is operative in other states without entering any decree in such states.⁶⁸

§ 5568. Effect on tenure of office and powers of corporate officers. The president of a corporation whose charter has been annulled for failure to pay taxes has no authority to act, and his acts cannot be ratified by the corporation.⁶⁹ Under the New Jersey statute making directors trustees on dissolution of a corporation, the president cannot assign a patent after a repeal of the charter.⁷⁰ Liquidation of a national bank does not terminate its corporate existence nor the authority of its cashier.⁷¹

§ 5572. Effect on right to continue business as a going concern. A dissolved corporation cannot continue business as a going concern.⁷² Where a charter is repealed by the governor under the New Jersey statutes for failure to pay taxes, but without the knowledge of the corporate officers, they are not personally liable on contracts thereafter made by them for the corporation in good faith.⁷³ There is only one cause of action, and not an improper joinder of causes of action, where all the directors united in an unlawful common purpose to carry on the business of a dissolved corporation instead of winding it up.⁷⁴

⁶⁷ *Miller v. American Bank & Trust Co.*, — W. Va. —, 100 S. E. 864.

⁶⁸ *Siegel v. Maryland Casualty Co.*, 178 N. Y. Supp. 391.

⁶⁹ *Houston v. Utah Lake Land, Water & Power Co.*, — Utah —, 187 Pac. 174.

⁷⁰ *Burgess Battery Co. v. Solar Light Co.*, 266 Fed. 368.

⁷¹ *Fagan v. Texas Co.*, — Tex. Civ. App. —, 220 S. W. 346.

⁷² *Houston v. Utah Lake Land, Water & Power Co.*, — Utah —, 187 Pac. 174, quoting *Fletcher Cyc. Corp.* § 5572.

⁷³ *Held v. Crosthwaite*, 260 Fed. 613 (but see dissenting opinion of Judge Rogers).

⁷⁴ *Wilson v. Brown*, 107 N. Y. Misc. 167, 175 N. Y. Supp. 688.

§ 5575. Effect on power to contract.⁷⁵ Where a corporate charter was repealed by the governor, under the New Jersey statute, for failure to pay taxes, officers of the corporation who continued the business without knowledge of the repeal are not personally liable on contracts made by them for the company which was afterwards reinstated by proclamation of the governor.⁷⁶ Persons dealing with a corporation whose charter has been annulled for failure to pay taxes cannot enforce such contracts although they were ignorant of the annulment.⁷⁷

§ 5578. Effect of dissolution on existing contracts—In general. The dissolution of a corporation gives no relief from liability on its existing contracts, and the corporate assets must satisfy such liabilities before they can be distributed.⁷⁸

§ 5579. — Where dissolution is voluntary. Voluntary dissolution of a corporation results in the annulment of existing contracts so far as executory, and recovery is not limited to the damages accruing up to the time of the dissolution.⁷⁹ Voluntary liquidation of an insolvent corporation is a breach of a continuing contract of employment where the employment is thereby terminated.⁸⁰

§ 5583. — Leases. Where a special statute dissolving a corporation gives it three years to wind up the business, a lease to the corporation is not terminated thereby before the end of the three years.⁸¹

§ 5591. Effect on stockholders—Vesting of title to corporate assets in stockholders. After dissolution, property of the corporation becomes vested in the stockholders subject to the rights of creditors; and if there are no creditors, the stockholders are

⁷⁵ See also § 5568, *supra*.

⁷⁶ *Held v. Crosthwaite*, 260 Fed. 613, Judge Rogers dissenting in separate opinion.

⁷⁷ *Houston v. Utah Lake Land, Water & Power Co.*, — *Utah* —, 187 Pac. 174.

⁷⁸ *Okmulgee Window Glass Co. v. Frink*, 260 Fed. 159.

⁷⁹ *Okmulgee Window Glass Co. v. Frink*, 260 Fed. 159.

⁸⁰ *Reigate v. Union Mfg. Co. (Ramsbottom), Ltd.*, [1918] 1 K. B. 592.

⁸¹ *Conn v. Manchester Amusement Co.*, — *N. H.* —, 111 Atl. 339.

the owners of the property.⁸² In Montana, on dissolution, stockholders, as against third persons, stand in a relationship of tenants in common, and may assert a legal as well as an equitable title.⁸³

A deed by a stockholder, after dissolution of the corporation, conveys his interest subject to the rights and powers of the trustees in settling the corporate affairs, and hence the deed affords no basis for a judgment quieting title as against the trustees.⁸⁴

§ 5593. Effect of dissolution as regards corporate property and conveyances—Modern rule. Property does not escheat on dissolution,⁸⁵ and corporate land does not revert to the grantor.⁸⁶

§ 5601. Effect on power of corporation to sue or to be sued—Rule independently of statute. A cause of action in favor of a corporation to recover its property does not abate on dissolution of the corporation but merely becomes vested in the statutory trustees.⁸⁷

§ 5605. — Rule under modern statutes. Generally the right to sue or be sued is conferred by a statute extending the corporate existence for a limited time.⁸⁸ Under the Colorado statute, an action may be maintained against a corporation after its dissolution, where the cause of action arose prior thereto.⁸⁹

⁸² *Smyth v. Kenwood Land Co.*, — Ore. —, 190 Pac. 962.

Where there are no creditors, the stockholders of a dissolved corporation are the equitable owners of all the corporate property. *De Martini v. McCaldin*, 184 N. Y. App. Div. 222, 171 N. Y. Supp. 528, rev'g on other grounds 101 N. Y. Misc. 304, 167 N. Y. Supp. 596.

On dissolution, title to the corporate property vests in the stockholders subject to the payment of the debts and liabilities of the corporation. *Young v. Fitch*, 182 Ky. 29, 206 S. W. 29.

⁸³ *Barker v. Edwards*, 259 Fed. 484.

⁸⁴ *Anthony v. Janssen*, — Cal. —, 191 Pac. 538.

⁸⁵ *Gulf Lines Connecting Ry. v. Golconda Northern Ry.*, 290 Ill. 384, 125 N. E. 357.

⁸⁶ *Root v. Wear*, 98 Kan. 234, 157 Pac. 1181.

⁸⁷ *Holmes v. Camp*, 186 N. Y. App. Div. 675, 175 N. Y. Supp. 349.

⁸⁸ *Matson v. Kennecott Mines Co.*, 101 Wash. 12, 171 Pac. 1040, holding that Nevada statute is not confined in its operation to that state.

⁸⁹ *Lucifer Coal Co. v. Buster*, 64 Colo. 179, 171 Pac. 61.

A national bank, even though in process of liquidation, may sue and be sued in its own name until its affairs are settled.⁹⁰ Dissolution does not affect the power of a corporation to enforce its rights, under Alabama statutes.⁹¹

§ 5607. — Proper or necessary parties to action. If a corporation whose charter has expired is in fact an existing corporation, it and not its stockholders is the proper party to sue, at least unless the corporation refuses to sue.⁹²

§ 5611. Judgment and execution after dissolution. A judgment against a corporation is void where the corporation was dissolved before the commencement of the action.⁹³ A stockholder of a dissolved corporation, while ordinarily entitled to attack a judgment against the corporation void because the corporation was dissolved before the action resulting in such judgment was commenced, is estopped to do so where his acts induced the prosecution of the action to final judgment.⁹⁴ Dissolution of a corporation does not, under the New York statutes continuing the existence of dissolved corporations for the purpose of satisfying existing debts, etc., preclude supplementary proceedings to enforce a judgment after the dissolution, and the order may be served on the president who may be required to appear.⁹⁵

§ 5612. Appeal or writ of error after dissolution. Where a corporation is dissolved *pendente lite*, appeals may be taken and a notice of appeal served on the directors.⁹⁶

§ 5613. Effect of dissolution *pendente lite*—Independently of statute. In some states, judgment cannot be entered against a dissolved corporation although the action was pending at the time of the dissolution,⁹⁷ but it has been held that dissolution

⁹⁰ *Farmers' Nat. Bank v. Johnston*, — Okla. —, 176 Pac. 236.

⁹¹ *Zadek v. Merchants' Bank*, — Ala. —, 85 So. 552.

⁹² *Rossing v. State Bank*, 181 Iowa 1013, 165 N. W. 254.

⁹³ *California Nat. Supply Co. v. Flack*, — Cal. —, 190 Pac. 634; *Slayden v. O'Dea*, — Cal. App. —, 189 Pac. 1062.

⁹⁴ *Slayden v. O'Dea*, — Cal. App. —, 189 Pac. 1062.

⁹⁵ *Sanitary Brass Works v. Rubin & Marcus*, 110 N. Y. Misc. 565, 180 N. Y. Supp. 619.

⁹⁶ *Slayden v. O'Dea*, — Cal. App. —, 189 Pac. 1062.

⁹⁷ *White v. Texas Motorear & Supply Co.*, — Tex. Civ. App. —, 203 S. W. 441.

of defendant corporation does not preclude entry of a judgment *nunc pro tunc* against it.⁹⁸ Pleadings filed by a defendant corporation after its dissolution by expiration of time are nullities.⁹⁹ Where a corporation is dissolved pending an action against it, papers cannot thereafter be served on its attorney.¹

§ 5614. — Statutory provisions. Dissolution does not abate pending suits against the corporation, under modern statutes.² Dissolution does not abate an action against the corporation for unliquidated damages, under the Arkansas statute.³

§ 5616. — Statutes as applicable to foreign corporations.⁴

§ 5617. — Substitution of parties. In California, where a corporation is dissolved *pendente lite*, even if the action does not abate, the proper persons must be substituted for the corporation.⁵ In that state, dissolution of defendant corporation pending the action can be brought to the attention of the court only on a proper suggestion made by someone other than the defunct corporation.⁶ But substitution of parties is not necessary, where a corporation becomes defunct *pendente lite* because of failure to pay the license tax.⁷ In Delaware, if a corporation is dissolved for nonpayment of a franchise tax while a suit is pending against it, the suit does not abate and the stat-

⁹⁸ Florida Development Co. v. Polk County Nat. Bank, 76 Fla. 629, 80 So. 560.

⁹⁹ Nezik v. Cole, — Cal. App. —, 184 Pac. 523.

¹ Nezik v. Cole, — Cal. App. —, 184 Pac. 523.

² Des Arc Oil Mill Co. v. McLeod, 141 Ark. 332, 216 S. W. 1040; Sanitary Brass Works v. Rubin & Marcus, 110 N. Y. Misc. 565, 180 N. Y. Supp. 619; Butcher v. J. I. Case Threshing Machine Co., — Tex. Civ. App. —, 207 S. W. 980.

³ Des Arc Oil Mill Co. v. McLeod, 141 Ark. 332, 216 S. W. 1040.

An action at law pending

against a corporation at the time of its dissolution need not be transferred to the chancery court where a receivership was pending. Des Arc Oil Mill Co. v. McLeod, 141 Ark. 332, 216 S. W. 1040.

⁴ See § 5810, *infra*.

⁵ Nezik v. Cole, — Cal. App. —, 184 Pac. 523.

If a corporation is dissolved pending an action against it, its directors, as statutory trustees, must be substituted as defendants. Nezik v. Cole, — Cal. App. —, 184 Pac. 523.

⁶ Nezik v. Cole, — Cal. App. —, 184 Pac. 523.

⁷ Slayden v. O'Dea, — Cal. App. —, 189 Pac. 1062.

utory trustees need not be substituted for the corporation, since the statute continues corporate existence for three years after dissolution and the statute relating to substitution of parties applies only to voluntary dissolutions.⁸

VIII. PROCEDURE AND ACTS CONNECTED WITH WINDING UP

A. In General

§ 5620. Statutory provisions for winding up. Dissolution of banks and trust companies is often specially provided for, at least so far as the procedure is concerned.⁹ Where the statutes provide for the manner of winding up a fraternal insurance company, by quo warranto proceedings by the attorney general, such remedy is exclusive and the provision therefor is a part of the contract between the society and its members, so as to bar an action by a member for a receiver and dissolution.¹⁰

§ 5624. Right of stockholders to sue after dissolution. Stockholders of a dissolved corporation may sue a third person as a trustee ex maleficio where there are no creditors, and a receiver need not be joined as a party.¹¹ A stockholders' suit by stockholders of a subsidiary company, not only on behalf of the subsidiary corporation but also indirectly for the benefit of the holding company, was held not abated by dissolution of the subsidiary corporation, and it was also held that the statutory trustees need not be substituted as plaintiffs where such trustees were the directors at the time of the dissolution.¹²

§ 5625. Sale of property in connection with winding up. A solvent corporation should not be enjoined by a federal court from selling its property in dissolution proceedings in a state court, at the suit of one claiming damages for patent infringements.¹³

⁸ *Townsend v. Delaware Glue Co.*, — Del. —, 103 Atl. 576.

⁹ *Montgomery Bank & Trust Co. v. State*, 201 Ala. 447, 78 So. 825.

¹⁰ *Cummings v. Supreme Council of Royal Arcanum*, 247 Fed. 992.

¹¹ *De Martini v. McCaldin*, 184 N. Y. App. Div. 222, 171 N. Y. Supp. 528, rev'g 101 N. Y. Misc.

304, 167 N. Y. Supp. 596, as set forth in vol. 8, note 83.

¹² *Holmes v. Camp*, 186 N. Y. App. Div. 675, 175 N. Y. Supp. 349.

¹³ *Window Glass Mach. Co. v. New Bethlehem Window Glass Co.*, 264 Fed. 822.

B. Statutory Continuation of Corporate Life for Limited Time After Dissolution

§ 5628. **Statutes generally.** After dissolution, there is a qualified existence for winding up purposes.¹⁴ Under the New York statutes, a dissolved corporation continues in existence for the purpose of enforcing a judgment against it by supplementary proceedings.¹⁵

§ 5630. **Statutes as confined to certain kind of dissolution.** Statutory provisions for continuing the corporate life for a limited time for winding up purposes do not, in New York, apply to a dissolution because of the expiration of the charter.¹⁶

§ 5632. **Length of continuation.** Where a statute provides that on dissolution for certain causes the corporation "may thereafter continue to act for the purpose of closing up its business but for no other purpose," but does not fix the time for which the life of the corporation shall be extended, directors may sue to obtain a sale of the property although some two years have elapsed since the dissolution, where the delay has worked no injustice.¹⁷

§ 5636. **Statute as conferring particular powers—To engage in new business.** Such a statute does not authorize the corporation to engage in a new business.¹⁸

C. Trustees for Purpose of Winding Up

§ 5639. **In general.** Statutes often make directors trustees to wind up the dissolved corporation.¹⁹ Statutory trustees are not

¹⁴ *Irons v. Croft Hat & Notion Co.*, — W. Va. —, 104 S. E. 111.

¹⁵ *Sanitary Brass Works v. Rubin & Marcus*, 110 N. Y. Misc. 565, 180 N. Y. Supp. 619.

¹⁶ *Wilson v. Brown*, 107 N. Y. Misc. 167, 175 N. Y. Supp. 688.

¹⁷ *Young v. Fitch*, 182 Ky. 29, 206 S. W. 29.

¹⁸ New business after forfeiture

of the charter is void and cannot be ratified; and this includes the purchase of stock in another corporation. *Houston v. Utah Lake Land, Water & Power Co.*, — Utah —, 187 Pac. 174, quoting *Fletcher Cyc. Corp.* § 5636.

¹⁹ *American Cotton Oil Co. v. Saluda Oil Mill Co.*, 107 S. C. 422, 93 S. E. 14.

officers of the court but are merely statutory liquidators.²⁰ The California statute making directors trustees on dissolution does not apply to a "suspension" of rights under the 1917 statute for failure to pay a license tax.²¹

§ 5643. Number necessary to act. Where directors become statutory trustees, on dissolution, a deed by one of them alone transfers no title unless executed pursuant to the direction of the directors acting unitedly.²² But where all the statutory trustees (directors), except one, had abandoned the trust and left the country, his acts as such are binding where ratified by subsequent conduct of the absent trustees.²³

§ 5644. Interference with by court. Statutory trustees should not be removed where not necessary to protect the corporate assets.²⁴

§ 5645. Powers and rights of trustees—In general. Directors, as statutory trustees after dissolution, may execute their powers without the interposition of any court.²⁵ They have power to engage in any lawful business.²⁶ Where a statute provides that in case of forfeiture all the assets shall be held in trust by the directors, and another statute provides for continuation of corporate life to wind up affairs, directors have power, after forfeiture, as trustees, to confess a judgment on a debt.²⁷

§ 5646. — Title to corporate property and control thereof.²⁸ On dissolution, directors who become statutory trustees do not

²⁰ *Holmes v. Camp*, 186 N. Y. App. Div. 675, 175 N. Y. Supp. 349.

²¹ *Siegel v. Maryland Casualty Co.*, 178 N. Y. Supp. 391.

The California statutes making directors, at the time of dissolution, trustees, apply to corporations dissolved for nonpayment of license taxes. This was held under an earlier statute. *Hanson v. Choyanski*, 180 Cal. 275, 180 Pac. 816.

²² *Anthony v. Janssen*, — Cal. —, 191 Pac. 538.

²³ *Bunn v. City of Laredo*, — Tex. Civ. App. —, 213 S. W. 320.

²⁴ *Langer v. Fargo Mercantile Co.*, — N. D. —, 174 N. W. 90.

²⁵ *Crystal Pier Co. v. Schneider*, 40 Cal. App. 379, 180 Pac. 948.

²⁶ See *Clark v. Groger*, 102 Wash. 188, 172 Pac. 1164.

²⁷ *Henriod v. East Tintic Development Co.*, 52 Utah 245, 173 Pac. 134.

²⁸ Right of statutory trustees to sue to recover corporate property, under Texas railroad statute, see *Richardson v. Allison*, — Tex. —,

acquire title to the corporate assets but only the right of possession;²⁹ but an assignment made by statutory trustees passes the title of the corporation.³⁰ Power conferred on directors as statutory trustees "to settle the affairs of the corporation" includes power to sell the corporate assets, which discretion will not be interfered with by the courts in the absence of fraud or collusion.³¹

§ 5650. Actions and parties thereto. On dissolution, statutory trustees must be sued jointly, to establish a corporate liability.³² In a suit by directors concerning the sale of property of a dissolved corporation, and to distribute the proceeds, all the stockholders need not be joined as parties.³³ Stockholders of a dissolved corporation may sue trustees for an accounting without joining a receiver as a party, where there are no creditors.³⁴

§ 5651. Compensation of trustees. If statutory trustees render no services, they are not entitled to any compensation.³⁵ Where one corporation turns over all its assets to another company for liquidation, and appoints an agent to assist the transferee which accepts his services, he may sue the transferee for the value of his services.³⁶

D. Receivers

§ 5659. Appointment—Appointment as substitute for corporate officers made statutory trustees or for liquidator chosen by stockholders. A receiver is not necessary, after dissolution, to take the place of directors as trustees, where there is no showing of fraud or bad faith.³⁷

213 S. W. 252, rev'g —Tex. Civ. App. —, 171 S. W. 1021.

²⁹ Crystal Pier Co. v. Schneider, 40 Cal. App. 379, 180 Pac. 948.

³⁰ Binford v. Boyd, 178 Cal. 458, 174 Pac. 56.

³¹ Crystal Pier Co. v. Schneider, 40 Cal. App. 379, 180 Pac. 948.

³² Leyhe v. Leyhe, — Tex. Civ. App. —, 220 S. W. 377.

³³ Young v. Fitch, 182 Ky. 29, 206 S. W. 29.

³⁴ See De Martini v. McCaldin, 184 N. Y. App. Div. 222, 171 N. Y. Supp. 528, rev'g 101 N. Y. Misc. 304, 167 N. Y. Supp. 596.

³⁵ Fratessa v. Morrissey, 39 Cal. App. 131, 178 Pac. 303.

³⁶ Anderson v. American Nat. Bank, 149 Ga. 798, 102 S. E. 534.

³⁷ Henriod v. East Tintic Development Co., 52 Utah 245, 173 Pac. 134.

§ 5670. **Title of receiver to corporate property.** In Illinois, a statutory receiver appointed on dissolution takes title to all the corporate assets wherever situated.³⁸

§ 5679. **Joinder or substitution as party in pending action.** A receiver should not be ordered to appear and answer in an action at law against his corporation, where there is nothing to indicate it will promote the winding up of the company.³⁹

E. Rules Governing Distribution

§ 5685. **Priorities and payment of claims—Amounts and equities as determinable as of what time.** A creditor or claimant cannot participate unless his claim was fixed or determinable at the time the corporation was dissolved; and the statutory provision continuing corporations in existence for a limited time after dissolution does not extend the right to sue such corporations on debts not in existence at the time of the dissolution.⁴⁰

³⁸ Hopkins v. Lancaster, 254 Fed. 190.

³⁹ Stewart v. Stewart Drug Co., 117 Me. 84, 102 Atl. 823.

⁴⁰ City of New York v. New York & South Brooklyn Ferry & Steam Transp. Co., 104 N. Y. Misc. 438, 172 N. Y. Supp. 495.

CHAPTER 65

FOREIGN CORPORATIONS

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I. DEFINITION AND NATURE OF FOREIGN CORPORATIONS

§ 5703. Ownership of corporate stock not controlling feature.¹

§ 5705. Status of foreign corporation as citizen, resident or inhabitant. A foreign corporation complying with state laws is nevertheless a "nonresident" of the county within a statute fixing the time to appeal from the decision of a justice of the peace.² However, statutes requiring registration of automobiles of "non-residents" do not apply to automobiles of foreign corporations doing business in the state.³

II. DOMESTICATION OF FOREIGN CORPORATIONS

§ 5707. Corporations under the laws of different states. A corporation created in one state may be made a corporation of another state by appropriate legislation, so that the laws as to foreign corporations will not apply.⁴

¹ See § 22 et seq., supra.

² Donohue v. Southwestern Surety Ins. Co., — Mo. —, 219 S. W. 930.

³ Gondek v. Cudahy Packing Co., 233 Mass. 105, 123 N. E. 398.

⁴ Proprietors of Cornish Bridge v. Fitts, — N. H. —, 107 Atl. 626.

III. POWER OF CORPORATION TO ACT IN FOREIGN STATE

§ 5720. Restrictions and limitations of charter.⁵

§ 5722. Restrictions in general legislation or judicial decisions of domicile. Laws of a state which become a part of the charter of a corporation and follow the corporation when it engages in business in another state are to be distinguished from laws regulating the manner of doing corporate business which are not extraterritorial.⁶

§ 5730. By what law corporate powers and acts of foreign corporation governed. A fire insurance company transacting business in a foreign state is bound, in respect to such business, by the laws of the state where the business is transacted.⁷

The power to issue stock, or to increase the stock, is governed by the laws of the state where the corporation is created.⁸ Issuing of stock is a corporate act controlled by the laws of the incorporating state, and the public service commission cannot authorize an increase of stock by a foreign corporation.⁹ But foreign corporations granted a permit to do business in Iowa are bound by the Iowa statutes as to the power to issue stock below par, where the permit expressly provides that it subjects the company to all statutes of Iowa relating to organization for pecuniary profit.¹⁰

IV. DOCTRINE OF COMITY TOWARDS FOREIGN CORPORATIONS

§ 5734. Right of corporation to act in another state or country. A state may prescribe the terms upon which alone it will permit foreign corporations to do business within its borders.¹¹ It may impose any conditions it desires.¹² Foreign cor-

⁵ See § 5740, *infra*.

⁶ *Washington-Alaska Bank v. Dexter Horton Nat. Bank*, 263 Fed. 304.

⁷ *American Fire Ins. Co. v. King Lumber & Manufacturing Co.*, 250 U. S. 2, 63 L. Ed. 810, *aff'd* 74 Fla. 130, 77 So. 168.

⁸ *In re Fryeburg Water Co.*, — N. H. —, 106 Atl. 225.

⁹ *In re Fryeburg Water Co.*, — N. H. —, 106 Atl. 225.

¹⁰ *Tramp v. Marquesen*, — Iowa —, 176 N. W. 977.

¹¹ *Kluver v. Middlewest Grain Co.*, — N. D. —, 173 N. W. 468.

¹² *Indiana Harbor Belt R. Co. v. Green*, 289 Ill. 81, 124 N. E. 298; *Dixon v. Northwestern Nat. Life*

porations may be compelled to take out a license as a condition of doing business.¹³

§ 5736. Application of the doctrine of comity to corporations.¹⁴

§ 5740. Limitation of comity by local policy.¹⁵ Where a state does not provide for the granting of a charter to domestic corporations of a certain character, such nonaction on its part is not in the nature of a prohibition against foreign corporations created for such purpose.¹⁶ An intent to exclude foreign corporations from a state is not shown by the fact that the laws of the state have made no provision for the creation of domestic corporations of like character.¹⁷ A foreign corporation cannot be refused permission to do business in Kansas because its shares of stock are without any nominal or par value.¹⁸

A statute forbidding the license of foreign corporations which could not be organized under the local laws excludes only those foreign companies whose purposes or manner of organization contravene some public policy of the state, and does not exclude corporations whose stock is issued without any stated par value.¹⁹

Ins. Co., — Iowa —, 179 N. W. 885.

Where interstate commerce is not directly affected, a state may forbid foreign corporations from doing business or acquiring property within her borders except on compliance with state statutes as to filing the charter, etc. *Munday v. Wisconsin Trust Co.*, 252 U. S. 499, 64 L. Ed. 684, aff'g *Munday v. Walter*, 168 Wis. 31, 168 N. W. 393, 169 N. W. 612.

¹³ *Great West Saddlery Co. v. Davidson*, 48 Dom. L. Rep. (Can.) 404.

¹⁴ The sources of evidence of public policy of the state as to foreign corporations restated in *State ex rel. Standard Tank Car Co. v. Sullivan*, — Mo. —, 221

S. W. 728, citing and quoting *Fletcher Cyc. Corp.* § 5736.

¹⁵ See also § 5743, *infra*.

¹⁶ *Stump v. Sturm*, 254 Fed. 535, rev'g on other grounds 239 Fed. 749.

¹⁷ *State ex rel. Standard Tank Car Co. v. Sullivan*, — Mo. —, 221 S. W. 728, citing *Fletcher Cyc. Corp.* § 5740.

¹⁸ *North American Petroleum Co. v. Hopkins*, 105 Kan. 161, 181 Pac. 625.

¹⁹ A foreign corporation is not to be excluded merely because its capital stock is of a kind not provided for by the local statutes. *State ex rel. Standard Tank Car Co. v. Sullivan*, — Mo. —, 221 S. W. 728.

§ 5743. **Comity as restricting foreign corporations to powers exercisable by similar domestic corporations.** Comity does not require that foreign corporations be given any greater privileges in making contracts within the state than are accorded to similar domestic corporations.²⁰ A contract involving real estate transactions, made by a Virginia corporation and within its charter powers, is legal in the District of Columbia although a company created therein cannot engage in the real estate business.²¹

A foreign corporation cannot exercise the rights and powers of a building and loan association, so as to escape usury laws, unless created under a materially identical or similar statute as the one in the local state and unless the character of its business is substantially the same as that conducted by such associations in the local state.²²

§ 5748. **Right of foreign corporation to sue under doctrine of comity.** The principle of comity entitles a foreign trust company to sue in Maryland to enforce or protect its rights in trust property.²³

V. CONSTITUTIONAL PROTECTION OF FOREIGN CORPORATION

§ 5754. **Corporations not entitled to privileges and immunities of citizens of the several states and of the United States.**²⁴

§ 5755. **Protection against denial of equal protection of the laws.**²⁵ Statutes permitting adverse examination of officers of foreign corporation suing in the state, and permitting a dismissal for refusal to be examined and to produce papers, do not deny equal protection of the laws to foreign corporations nor violate the due process of law provision.²⁶

²⁰ *Holt v. Aetna Building & Loan Ass'n*, 78 Okla. 307, 190 Pac. 872; *Union Sav. Ass'n v. Cummins*, 78 Okla. 265, 190 Pac. 869.

²¹ *Hight v. Richmond Park Improvement Co.*, 47 App. Cas. (D. C.) 518, and see § 5740, *supra*.

²² *Midland Savings & Loan Co. v. Nicoll*, 76 Okla. 27, 183 Pac. 731.

²³ *Baden v. Washington Loan & Trust Co.*, 133 Md. 602, 105 Atl. 800.

²⁴ See § 389, *supra*.

²⁵ See §§ 4403-4415, *supra*.

²⁶ *Kentucky Finance Co. v. Allen*, — Wis. —, 178 N. W. 9.

§ 5757. Statutes impairing obligation of contracts or affecting vested rights.²⁷ Termination of authority of a foreign corporation to do business in a state does not prevent subsequent enforcement in such state of liability incurred while authorized to do business therein.²⁸

§ 5763. Restrictions upon foreign corporations engaged in interstate commerce.²⁹ Statutes relating to foreign corporations do not apply so far as the corporation is engaged in interstate commerce.³⁰ It follows that no permit or license or authority is necessary to enable a corporation to do business constituting interstate commerce, outside the state of its creation;³¹ and the fact that a foreign corporation is doing business in the state, in such manner as to require a license therefor, does not prevent it from performing other acts in interstate commerce without a license.³² So a foreign corporation, without obtaining a permit to do business, may sue on a note given for a debt incurred in the transaction of interstate commerce,³³ or may sue to enforce payment for goods sold in interstate commerce to residents.³⁴

A contract involves interstate commerce so as not to be within the Michigan statutes relating to doing of business by foreign corporations, where thereunder a foreign corporation not authorized to do business in Michigan agrees to become the sales agent for the whole United States for a Michigan concern.³⁵

§ 5764. Construction of statutes as not being applicable to interstate commerce.³⁶ The Massachusetts statute exacting a fee of five dollars from foreign corporations for filing annual certificates of condition is not unreasonable, but does not apply

²⁷ See also § 5914, *infra*.

²⁸ *American Fidelity Co. v. Leahy*, 189 N. Y. App. Div. 242, 178 N. Y. Supp. 511.

²⁹ See also § 5767, *infra*.

³⁰ *Campbell Elec. Co. v. Christian*, 141 Minn. 296, 170 N. W. 199.

³¹ *Fennell v. Trinity Portland Cement Co.*, — Tex. Civ. App. —, 209 S. W. 796.

³² *Gutta Percha Manufacturing*

& Rubber Co. v. Lehrack, 201 Mo. App. 550, 214 S. W. 285.

³³ *Crisp v. Christian Moerlein Brewing Co.*, — Tex. Civ. App. —, 212 S. W. 531.

³⁴ *American Brick & Tile Co. v. Turnell*, — Minn. —, 173 N. W. 175.

³⁵ *American Distributing Co. v. Hayes-Wheel Co.*, 250 Fed. 109.

³⁶ See also § 5763, *supra*.

to foreign corporations unless engaged in domestic business in the state.³⁷

§ 5765. Regulation of foreign corporation under police power of the state.³⁸

§ 5767. Corporations engaged in transportation of freight and passengers.³⁹

§ 5768. Telegraph and telephone companies.⁴⁰

§ 5770. Sales and traffic by foreign corporations. A contract for delivery of goods to a common carrier for transportation outside the state involves interstate commerce.⁴¹ An agreement by a foreign corporation to sell to a resident goods f. o. b. cars at its home office relates to interstate commerce.⁴² A sale of tile to be shipped from one state to another and delivered on board cars at the buyer's domicile is interstate commerce.⁴³ A sale within the state, by a foreign corporation, of goods located in another state where it has its principal place of business, which sale is followed by delivery and transportation, is interstate commerce which cannot be burdened by state legislation.⁴⁴ Selling its manufactured products through soliciting or sales agents on written orders taken in the state and forwarded to the factory in the home state for approval, constitutes interstate commerce for which no permit is necessary.⁴⁵ A sale is none the less inter-

³⁷ *Lever Bros. Co. v. Com.*, 232 Mass. 22, 121 N. E. 516.

³⁸ See § 4360 et seq., supra.

³⁹ Fee for issuing bonds, see § 5781, infra.

⁴⁰ See § 4453 et seq., supra.

⁴¹ *C. S. Martin & Son v. John Bonura & Co.*, — Tex. Civ. App. —, 214 S. W. 841. See also *W. W. Kimball & Co. v. Read*, — Cal. App. —, 185 Pac. 192.

Ordering goods by mail, and delivery on board cars in a foreign state, is interstate commerce which cannot be interfered with. *W. T. Rawleigh Co. v. Van Duyn*, 32 Idaho 767, 188 Pac. 945.

⁴² *J. R. Watkins Medical Co. v. Hunt*, — Neb. —, 177 N. W. 462.

A manufacturer is engaged in interstate commerce so as not to be required to take out a Texas license, where it sells medicines in Illinois to one in Texas to be delivered f. o. b. in Illinois. *W. T. Rawleigh Co. v. Marshall*, — Tex. Civ. App. —, 220 S. W. 1111.

⁴³ *American Brick & Tile Co. v. Turnell*, 143 Minn. 96, 173 N. W. 175.

⁴⁴ *Dahl Implement & Lumber Co. v. Campbell*, — N. D. —, 178 N. W. 197.

⁴⁵ *Deardorf v. Idaho Nat. Har-*

state commerce because collection therefor is made through a local agency.⁴⁶

Where the sale of certain articles of merchandise is merely incidental to a contract by a foreign corporation to carry on a "trade campaign" for a merchant, interstate commerce is not involved.⁴⁷ Sales by a baking company which sends its wagons across the state line where drivers sell and deliver bread is not interstate commerce.⁴⁸

§ 5774. Sales involving installation, construction, supervision or repair.⁴⁹ A contract by an Illinois company to install apparatus constructed in Illinois, shipped to Missouri, and there installed under the seller's supervision by local workmen, involves interstate commerce.⁵⁰ Sale and installation of a gasoline container and pump, involving employment of laborers in installation, is a transaction of business in the state.⁵¹ The equipment of a manufacturing plant with a sprinkler system is not interstate commerce, it is generally held,⁵² although some of the material was brought in from outside the state.⁵³ Installation of an ice plant has been held to be interstate commerce, in a particular case.⁵⁴

vester Co., 90 Ore. 425, 177 Pac. 33; *F. L. Shaw Co. v. Dalton Adding Mach. Co.*, — Tex. Civ. App. —, 211 S. W. 833.

⁴⁶ *Gutta Percha Manufacturing & Rubber Co. v. Lehrack*, 201 Mo. App. 550, 214 S. W. 285.

⁴⁷ *Dean v. Caldwell*, 141 Ark. 38, 216 S. W. 31.

⁴⁸ *Ward Baking Co. v. Federal Trade Commission*, 264 Fed. 330.

⁴⁹ The decision in the case of *General Ry. Signal Co. v. Com.*, 118 Va. 301, 87 S. E. 598, as stated on p. 9621, note 51 is affirmed in 246 U. S. 500, 62 L. Ed. 854.

A contract to furnish and erect ornamental plasterwork, where the work is not so complex as to prevent the sale unless erected by the seller, is a doing business in the state. *Decorators' Supply Co.*

v. Chaussee, 211 Mich. 302, 178 N. W. 665.

⁵⁰ *Hess Warming & Ventilating Co. v. Burlington Grain Elevator Co.*, — Mo. —, 217 S. W. 493.

⁵¹ *Bryan v. S. F. Bowser & Co.*, — Tex. Civ. App. —, 209 S. W. 189.

⁵² *United States Const. Co. v. Hamilton Nat. Bank*, — Ind. App. —, 126 N. E. 866.

A contract to equip a building with a fire sprinkler system, executed by a foreign corporation through subcontractors who manufactured and installed the system, was held not interstate commerce. *Phillips Co. v. Everett*, 262 Fed. 341.

⁵³ *In re Springfield Realty Co.*, 257 Fed. 785.

⁵⁴ *United Iron Works Co. v.*

§ 5775. Sale of stocks, bonds, securities and choses in action.⁵⁵

§ 5776. Insurance not commerce. The Kentucky statute regulating who may act as insurance agents in the state, as applied to foreign companies, is valid as merely imposing conditions on the right to act in the state.⁵⁶

§ 5781. Taxation of foreign corporation engaged in interstate commerce or acting as agent of federal government.⁵⁷ The Michigan statute providing that no foreign corporation shall make a contract in the state until compliance with provisions thereof does not impose a tax on interstate commerce where the franchise fee is based on the proportion of capital stock represented by the property owned and used and business transacted in Michigan.⁵⁸ Fixing a large charge for a certificate authorizing the issue of railroad bonds by the Union Pacific, a foreign corporation having only a small mileage in the state, based on a percentage of the whole issue, is an unlawful interference with interstate commerce.⁵⁹ As a condition to a public service commission granting authority to a railroad company to issue bonds, it cannot collect the statutory fee based on the total issue of bonds secured by mortgage on its entire system which is practically all outside the state, since thereby burdening interstate commerce.⁶⁰ A license tax computed according to the amount of sales of goods manufactured in the city, whether sold within or without the state, as applied to a foreign corporation, is not a regulation of interstate commerce and does not impose a tax upon property or business transactions outside the state so as to deprive the corporation of property without due process of law.⁶¹

Watterson Hotel Co., 182 Ky. 113, 206 S. W. 166.

The Texas case of York Mfg. Co. v. Colley as set forth in the text on page 9620 was reversed by the Supreme Court of the United States in York Mfg. Co. v. Colley, 247 U. S. 21, 62 L. Ed. 963, on the ground that interstate commerce was involved.

⁵⁵ Fees, see § 5781, *infra*.

⁵⁶ Adams v. Thomas, 246 Fed. 175.

⁵⁷ See also §§ 4585-4588, *supra*.

⁵⁸ Hayes Wheel Co. v. American Distributing Co., 257 Fed. 881.

⁵⁹ Union Pac. R. Co. v. Public Service Commission, 248 U. S. 67, 63 L. Ed. 131, rev'g 268 Mo. 641, 187 S. W. 827.

⁶⁰ Missouri Pac. R. Co. v. Public Utilities Commission, 292 Ill. 427, 127 N. E. 41.

⁶¹ American Mfg. Co. v. St. Louis, 250 U. S. 459, 63 L. Ed. 1084, *aff'g* — Mo. —, 198 S. W. 1183 (mem. dec.).

VI. REGULATION OF INTERNAL AFFAIRS OF FOREIGN CORPORATION

§ 5786. Courts have no visitorial power over a foreign corporation. Courts have no visitorial powers over foreign corporations,⁶² and cannot interfere with their internal management.⁶³

§ 5790. What controversies relate to internal management.⁶⁴

§ 5791. Power of courts to determine status of foreign corporation as de jure corporation. The status of a foreign corporation is governed by the laws of the state where doing business, rather than the laws of the state where created.⁶⁵

§ 5795. Right to inspect books of foreign corporation.⁶⁶

§ 5797. Power of courts in reference to stock and bonds of foreign corporation.⁶⁷ A transferee of stock may sue a foreign corporation to compel it to transfer his stock on its books, since not a matter relating to internal management so as to be cognizable only in the home state.⁶⁸ In an action to compel a foreign corporation to transfer stock on its books, an order compelling defendant to set out in words or substance the by-law under which it claimed a lien, does not involve the exercise of visitorial powers nor the management of the internal affairs of the corporation.⁶⁹

§ 5801. Power of courts of a state over dividends by a foreign corporation. In construing section 28 of the New York Stock Corporation Law making directors liable to the corporation or its creditors for dividends paid other than from surplus profits, in connection with section 70 of the same act making directors

⁶² *Tasler v. Peerless Tire Co.*, 144 Minn. 150, 174 N. W. 731; *In re Fryeburg Water Co.*, — N. H. —, 106 Atl. 225.

⁶³ *Richards v. Security Mut. Life Ins. Co.*, 230 Mass. 320, 119 N. E. 744; *Tasler v. Peerless Tire Co.*, 144 Minn. 150, 174 N. W. 731.

⁶⁴ See § 4065, *supra*.

⁶⁵ *State v. Atlantic Coast Line*

R. Co., 202 Ala. 558, 81 So. 60.

⁶⁶ See § 2825, *supra*.

⁶⁷ See also §§ 5730, 5781, *supra*.

⁶⁸ *Citizens' Nat. Bank v. Consolidated Glass Co.*, 83 W. Va. 1, 97 S. E. 689.

⁶⁹ *Baer v. Waseca Milling Co.*, 143 Minn. 483, 171 N. W. 767, 173 N. W. 401.

of foreign corporations liable "in the same manner and to the same extent" as the directors of a domestic corporation for paying unauthorized dividends, it is held that directors of a foreign corporation are liable for paying dividends other than from surplus profits, in an action in New York, although the corporation would not be liable in its home state; and that the statute, so far as applicable to foreign corporations, is within the power of the legislature and constitutional, and that the cause of action may be enforced by the foreign corporation itself.⁷⁰

§ 5803. Powers of courts as to officers of foreign corporation. Where a foreign corporation locates itself in a state and its managing officers are within the state, the courts of the state have jurisdiction to compel such officers to restore corporate assets wrongfully diverted.⁷¹

§ 5806. Extraterritorial enforcement of statutory liability for failure to file reports.⁷²

VII. DISSOLUTION OF FOREIGN CORPORATIONS

§ 5808. Power of legislature or courts to dissolve foreign corporations. A creditors' suit which is in effect an attempt to wind up a foreign corporation by the appointment of a receiver and collection of unpaid subscriptions, cannot be brought, since a corporation can be wound up only in the state where created.⁷³

§ 5810. Effect of dissolution of corporation by state of its domicile. Dissolution of a foreign corporation in its home state, where its principal place of business is in Kentucky, does not abate an action pending in Kentucky against the corporation, since the Kentucky statute under which actions do not abate on dissolution applies to both domestic and foreign corporations having their principal place of business in the state.⁷⁴

⁷⁰ German-American Coffee Co. v. Diehl, 216 N. Y. 57, 109 N. E. 875, rev'g 167 N. Y. App. Div. 928, 152 N. Y. Supp. 1113, and overruling, without noticing, De Raimes v. United States Lithograph Co., 161 N. Y. App. Div. 781, 146 N. Y. Supp. 813, set forth in Fletcher Cyc. Corp. § 5801, note 87.

⁷¹ Tasler v. Peerless Tire Co., 144 Minn. 150, 174 N. W. 731.

⁷² See § 2860, supra.

⁷³ Palmer v. Morgan, 45 App. Cas. (D. C.) 334.

⁷⁴ Hauger v. International Trading Co., 184 Ky. 794, 214 S. W. 438.

VIII. INSOLVENCY OF FOREIGN CORPORATION

§ 5823. Jurisdiction of local courts over insolvent foreign corporation. Where title to the property of an insolvent New York insurance company is vested by the New York statutes in the insurance commissioner, a Nebraska creditor cannot sue the company in the Nebraska courts, where it has been licensed to do business in Nebraska without any limitations in case of insolvency.⁷⁵

§ 5827. Preferential transfers and conveyances by foreign corporations. The New Jersey statute forbidding transfers when insolvent applies to a foreign corporation doing business in that state.⁷⁶

§ 5829. Discrimination against nonresident creditors. Resident creditors of foreign corporations ordinarily are not entitled to any priority over nonresident creditors.⁷⁷

IX. RECEIVERS OF FOREIGN CORPORATIONS

§ 5833. In general. A receiver may be appointed for a foreign corporation so far as assets located in the state are concerned.⁷⁸ A receiver may be appointed for the property in the state, in case of a foreign insurance company, where necessary to secure rights, although no authority exists to appoint a general receiver, and the court need not appoint merely an ancillary receiver.⁷⁹ Jurisdiction to appoint a receiver of an insolvent foreign corporation, to secure or preserve the assets within the state, does not depend upon whether there is a domiciliary receiver.⁸⁰

⁷⁵ *Kinsler v. Casualty Co. of America*, 103 Neb. 382, 172 N. W. 33.

⁷⁶ *Hoover Steel Ball Co. v. Schafer Ball Bearings Co.*, 89 N. J. Eq. 433, 105 Atl. 500.

⁷⁷ See note on this subject in 1 A. L. R. 648-650, annotating *Brunner v. York Bridge Co.*, 78 W. Va. 702, 1 A. L. R. 643, 90 S. E. 223.

⁷⁸ *Mitchell v. Banco de Londres*

y Mexico, 192 N. Y. App. Div. 720, 183 N. Y. Supp. 446. See also *People ex rel. Potts v. Continental Beneficial Ass'n*, 204 Ill. App. 501.

⁷⁹ *People ex rel. Potts v. Continental Beneficial Ass'n*, 289 Ill. 40, 124 N. E. 352, aff'g 212 Ill. App. 422.

⁸⁰ *Atwater v. Baskerville*, 90 N. J. Eq. 275, 106 Atl. 369.

Minority stockholders may sue for a receivership where the management is diverting corporate assets to their own use, although the company is a foreign corporation.⁸¹

The existence of corporate assets need not first be established to warrant the appointment of a receiver for a foreign corporation.⁸²

A creditor need not be a judgment creditor to be entitled to a receivership of the assets of a foreign corporation located in the state.⁸³

§ 5834. Effect of appointment of receiver for foreign corporation. Receivers of foreign corporations cannot be authorized to take charge of assets located outside the state.⁸⁴ A receiver of a foreign corporation stands in the shoes of the corporation, and cannot sue where the corporation could not sue because of failure to appoint a person on whom process may be served as required by statute.⁸⁵ Under the Rhode Island statutes, the court may authorize a receiver of a foreign corporation to carry on the business temporarily, with the incidental power to borrow money for the corporate enterprise.⁸⁶

§ 5837. Right of domiciliary receiver to sue in another jurisdiction.⁸⁷

§ 5844. Control and administration of assets of foreign corporation by ancillary receiver.⁸⁸

§ 5845. Conflict of jurisdiction between courts.⁸⁹ A Pennsylvania court, and therefore a federal court sitting within the

⁸¹ *Tasler v. Peerless Tire Co.*, 144 Minn. 150, 174 N. W. 731.

⁸² *Parten v. Southern Colonization Co.*, — Minn. —, 178 N. W. 744, and see § 5266, *supra*.

⁸³ *Mitchell v. Banco de Londres y Mexico*, 192 N. Y. App. Div. 720, 183 N. Y. Supp. 446.

⁸⁴ *Tasler v. Peerless Tire Co.*, 144 Minn. 150, 174 N. W. 731, holding, however, that failure to charge the receiver to take possession only of assets within the

state does not oust the court of jurisdiction nor affect the validity of the appointment of the receiver.

⁸⁵ *Frank v. Broadway Tire Exch. Co.*, — R. I. —, 105 Atl. 177.

⁸⁶ *Fairechild v. Uniform Seamless Wire Co.*, — R. I. —, 107 Atl. 201.

⁸⁷ See § 5327, *supra*.

⁸⁸ See § 5834, *supra*.

⁸⁹ See also § 5217, *supra*.

state, has power to appoint a receiver for a New Jersey corporation controlling many subsidiaries and carrying on its principal business in Pennsylvania.⁹⁰

X. POWER AND RIGHTS OF FOREIGN CORPORATIONS REGARDING PROPERTY

§ 5850. Power of foreign corporations to acquire and hold stock in domestic corporations.⁹¹

§ 5851. Acquisition and holding of real property by foreign corporation.⁹² There is no provision in West Virginia prohibiting foreign corporations from holding property in the state;⁹³ and a home missionary society, incorporated in another state, may hold property in West Virginia.⁹⁴

§ 5869. Devises to foreign corporations. A devise of land to a foreign corporation, such as a church, can be attacked only by the state as in violation of the public policy of the state as announced in its constitution.⁹⁵

§ 5873. Exercise of right of eminent domain by foreign corporation. A foreign corporation cannot condemn land unless authorized so to do by the laws of the state.⁹⁶ A foreign corporation which seeks to condemn land must by its petition show itself authorized so to do under and by virtue of the laws of the forum.⁹⁷ The Indiana statute conferring the power of eminent domain on railroad companies created by adjoining states applies where they became vested with title to railroad property partly in both states.⁹⁸

⁹⁰ Scattergood v. American Pipe & Construction Co., 249 Fed. 23.

⁹¹ See § 1125, *supra*.

⁹² Power to take lease, see § 1235, *supra*.

⁹³ Stump v. Sturm, 254 Fed. 535, *rev'g* on other grounds 239 Fed. 749.

⁹⁴ Stump v. Sturm, 254 Fed. 535.

⁹⁵ Stump v. Sturm, 254 Fed. 535, *rev'g* on other grounds 239 Fed. 749.

⁹⁶ Indiana Harbor Belt R. Co.

v. Green, 289 Ill. 81, 124 N. E. 298.

⁹⁷ Indiana Harbor Belt R. Co. v. Green, 289 Ill. 81, 124 N. E. 298.

In Illinois a foreign corporation cannot exercise the right of eminent domain under the general statute but only under Hurd's Rev. St. 1917, c. 114, § 218. Chicago, M. & St. P. R. Co. v. Franzen, 287 Ill. 346, 122 N. E. 492.

⁹⁸ Howard v. Illinois Cent. R. Co., 186 Ind. 88, 115 N. E. 50.

XII. TORTS AND CRIMES BY AND AGAINST FOREIGN CORPORATIONS

§ 5891. Doctrine where statute prohibits any suit by non-complying corporations.⁹⁹

XIII. STATUTES AND CONSTITUTIONAL PROVISIONS IMPOSING CONDITIONS AND RESTRICTIONS UPON FOREIGN CORPORATIONS

§ 5894. In general. As a condition of doing business in the state, foreign mutual insurance associations may be prohibited from issuing insurance to others than the classes designated in the statute.¹ Foreign building and loan associations, governed by special statutes, are not within the general statutes relating to foreign corporations.²

§ 5900. Statutes requiring payment of license fee or tax.³ So far as local business is involved, separate and distinct from interstate commerce, as in case of the instalment of an automatic railway signal system, the state may impose a license fee on a foreign corporation, provided it is reasonable.⁴

The "capital stock," a statement of the proportion of which represented in the state is required of foreign corporations as a basis of license taxes, means the capital stock authorized by the charter, whether issued or not.⁵ Where the fee for admission to the state to do business is based on the proportion of the "authorized capital stock" represented in the state, the fee must be based, where all the property is in the state, on the total authorized capital stock although in excess of the value of all the corporate property and of the issued stock.⁶ However, in Wisconsin, in determining the proportion of "capital stock" employed in Wisconsin, for the purpose of imposing license fees, "capital stock," as the term is used in the statute, means the actual, issued and paid-for stock and not merely the authorized

⁹⁹ See § 5967, *infra*.

¹ *Weiditschka v. Supreme Tent Knights of Maccabees*, — Iowa —, 175 N. W. 835.

² *Union Sav. Ass'n v. Burns*, — Okla. —, 176 Pac. 227.

³ See also § 5781, *supra*.

⁴ *General Ry. Signal Co. v. Vir-*

ginia, 246 U. S. 500, 62 L. Ed. 854, *aff'g* 118 Va. 301, 87 S. E. 598.

⁵ *American Can Co. v. Emmer-*
son, 288 Ill. 289, 123 N. E. 581.

⁶ *State ex rel. Bedford Coal By-*
Products Co. v. Fulton, 98 Ohio
St. 350, 121 N. E. 697.

amount of stock nor the measure of the assets or property of the corporation.⁷

Where an annual license tax on corporations is to be computed according to the proportion that the property owned and business transacted in the state bears to the aggregate amount of property owned and business transacted in and out of the state, the words "business transacted" means not only income but includes every kind of business transacted in the state.⁸

The 1917 statute in Illinois basing the fees required of foreign corporations on the per cent of its Illinois assets to its total assets and of its Illinois business to total business, is not such a change in computing fees as to violate the contract of the state with the corporation not to discriminate against foreign corporation.⁹

Mandamus lies in favor of a foreign corporation to compel the secretary of state to deliver to it the certificate authorizing it to do business, where the sole dispute is one of law as to fees, as to which the secretary of state is in the wrong.¹⁰

§ 5902. Statutes requiring designation of agent for the service of process. In appointing a person on whom process may be served, as required by statute, a foreign corporation cannot limit service on him to causes of action arising within the state.¹¹ A foreign corporation which has designated a person on whom process may be served is estopped to claim, where such person has been served, that the designation did not conform to the statute.¹² Under the New York statutes requiring foreign corporations to designate an agent on whom service may be made, service on such an agent is good although the cause of action arose in another state.¹³

⁷ *State v. Hull*, 168 Wis. 269, 169 N. W. 617.

⁸ *P. Lorillard Co. v. Scott*, 184 Ky. 312, 212 S. W. 145.

⁹ *American Can Co. v. Emmer-son*, 288 Ill. 289, 123 N. E. 581.

¹⁰ *State ex rel. Bedford Coal By-Products Co. v. Fulton*, 98 Ohio St. 350, 121 N. E. 697.

¹¹ *Sukosky v. Philadelphia & Reading Coal & Iron Co.*, 189 N.

Y. App. Div. 689, 179 N. Y. Supp. 23.

¹² *Sukosky v. Philadelphia & Reading Coal & Iron Co.*, 189 N. Y. App. Div. 689, 179 N. Y. Supp. 23.

¹³ *Philadelphia & Reading Coal & Iron Co. v. Kever*, 260 Fed. 534, following *Smolik v. Philadelphia & Reading Coal & Iron Co.*, 222 Fed. 148 and *Bagdon v. Philadel-*

§ 5903. Statutes requiring consent to service of process upon state officials. A foreign trust company authorized in its domicile to act as executor or administrator cannot so act in Connecticut except by compliance with the statute relating to appointment of secretary of state as its agent.¹⁴

§ 5904. Statutes requiring designation of agent for service of process and place of business. A state may require foreign corporations to maintain a known place of business within the state, with an agent residing there to receive service of process.¹⁵ Under the Constitution of Pennsylvania requiring foreign corporations doing business in the state to have one or more known places of business, and an authorized agent or agents therein on whom process may be served, a foreign corporation must have an authorized agent for service of process at every place in the state where it carries on business.¹⁶

§ 5910. Retaliatory constitutional or statutory provisions.¹⁷

§ 5914. Power of legislature to change statutes imposing conditions upon foreign corporations. A foreign corporation licensed to do business in the state at a time when a statute provided for equal treatment of domestic and foreign corporations, may complain of a subsequent statute discriminating against foreign corporations, as a violation of its contract.¹⁸ The California statutes imposing conditions on foreign corporations in

phia & Reading Coal & Iron Co., 217 N. Y. 432, L. R. A. 1916 F 407, Ann. Cas. 1918 A 389, 111 N. E. 1075.

¹⁴ Equitable Trust Co. v. Plume, 92 Conn. 649, 103 Atl. 940.

¹⁵ Hagler v. Security Mut. Life Ins. Co., 244 Fed. 863.

¹⁶ Carr v. Aetna Accident & Liability Co., 263 Pa. 87, 106 Atl. 107, rev'g 64 Pa. Super. Ct. 343.

¹⁷ Retaliatory legislation, construction of meaning of word "similar," see Fidelity & Deposit Co. v. Brown, 92 Vt. 390, 104 Atl. 234.

The reciprocity provision of the New Jersey Corporation Act imposing on foreign corporations "the same taxes, fines, penalties, licenses, fees, obligations and requirements of whatever kind" as are imposed by the laws of the state of foreign corporations on corporations of this state, construed as to right to sue on contracts made out of the state. Lehigh Structural Steel Co. v. Atlantic Smelting & Refining Works, — N. J. Eq. —, 111 Atl. 376.

¹⁸ American Can Co. v. Emmer-son, 288 Ill. 289, 123 N. E. 581.

existence before 1917 are inapplicable to actions or transactions after the 1917 repeal.¹⁹

XIV. APPLICATION OF STATUTORY AND CONSTITUTIONAL RESTRICTIONS AND REGULATIONS

§ 5916. In general.²⁰ The fact that a company owns stock in local subsidiary corporations does not bring it into the state in the sense of transacting its own business there.²¹

§ 5917. Whether corporation "doing business," a question of fact. The question as to whether a foreign corporation is doing business in the state is one of fact.²² Plaintiff is not entitled to a jury trial on a motion to quash the service of summons against a foreign corporation because it is not doing business in the state, etc.²³

§ 5918. Statutes generally applicable to foreign corporation transacting ordinary corporate business in state. A foreign corporation need not obtain a permit to do business unless actually doing business in the state.²⁴

§ 5919. Isolated or single transaction not doing business in a state. The transaction or doing of business within the state, within the prohibition of the statute relating to foreign corporations without compliance with certain requirements, does not cover a single business transaction or an isolated transaction.²⁵

¹⁹ *W. W. Kimball Co. v. Read*, — Cal. App. —, 185 Pac. 192.

²⁰ What constitutes "doing business" in general, see *Kernchen Co. v. English*, 70 Pa. Super. Ct. 293.

Doing business by soliciting agents as doing business in state, see also *Glynn v. Hyde-Murphy Co.*, 113 N. Y. Misc. 329, 184 N. Y. Supp. 462.

What constitutes doing business in state by foreign moving picture company, see *Rex Beach Pictures Co. v. Harry I. Garson Productions*, 209 Mich. 692, 177 N. W. 254.

²¹ *People's Tobacco Co. v. American Tobacco Co.*, 246 U. S. 79, 62 L. Ed. 587.

²² *Empire Fuel Co. v. Lyons*, 257 Fed. 890.

²³ *Williams v. J. F. Ball Bros. Lumber Co.*, 105 Kan. 284, 182 Pac. 552.

²⁴ *Houston Oil Co. v. W. R. Pickering Lumber Co.*, — Tex. Civ. App. —, 212 S. W. 802.

²⁵ *Hunau v. Northern Region Supply Corporation*, 262 Fed. 181; *Brioschi-Minuti Co. v. Elson-Williams Const. Co.*, — N. D. —, 172 N. W. 239; *Charles E. Walters Co.*

An isolated act of a foreign trust company in acting as trustee under a deed of trust and as such collecting interest, taking title to property, etc., does not constitute "carrying on business" within the state.²⁶ The making of a contract by a trust company administering a trust, to sell trust property in another state, is not "doing business" in that state, so as to bar an action because of failure to obtain the permit required of foreign corporations.²⁷

§ 5920. Doctrine that a single transaction may constitute doing business. "Doing business" does not necessarily require that it be done persistently and continuously.²⁸ While isolated acts ordinarily do not constitute "transacting business," yet a purchase of real estate to use as a place for its business is a transacting of business forbidden by statute before compliance with the local statutes.²⁹ Where a foreign corporation with its principal office near the state line has solicited business generally in tributary territory within the state, any transaction consummated by it in furtherance of its business is not an isolated transaction, within the rule that single or isolated acts do not constitute doing business.³⁰

§ 5921. Interstate commerce business not within purview of restrictive statutes. However, a corporation is doing business in the state, where it has a substantial local and domestic business entirely separate from, and not merely incidental to, its interstate business.³¹

§ 5922. Sales of goods through traveling salesmen or agents. A corporation is not doing business in another state, so as to be subject to statutes governing foreign corporations, merely

v. Hahn, — S. D. —, 178 N. W. 448.

A sporadic or occasional sale is not a doing of business. *Empire Fuel Co. v. Lyons*, 257 Fed. 890.

²⁶ *Equitable Trust Co. v. Western Land & Power Co.*, 38 Cal. App. 535, 176 Pac. 876.

²⁷ *Baden v. Washington Loan & Trust Co.*, 133 Md. 602, 105 Atl. 860.

²⁸ *Empire Fuel Co. v. Lyons*, 257 Fed. 890.

²⁹ *Lowenmeyer v. National Lumber Co.*, — Ind. App. —, 125 N. E. 67.

³⁰ *Dahl Implement & Lumber Co. v. Campbell*, — N. D. —, 178 N. W. 197.

³¹ *Hayes Wheel Co. v. American Distributing Co.*, 257 Fed. 881.

because it solicits orders through traveling salesmen and ships direct from the home state.³² A fortiori, mere solicitation of business by agents, without authority to conclude bargains, is not a doing of business.³³

A foreign corporation soliciting orders through a local salesman, shipping machines in response to the orders, after approval at the home office, and collecting for the shipments in the foreign state through its local salesmen, is doing business in the state, so as to be subject to service of process.³⁴

§ 5923. Sales of goods. A harvester company which sells parts through an agency in another state is doing business in the state.³⁵ Where a mining company sells a large part of its coal in another state through a coal company as its agent, it is doing business in such state.³⁶ A contract for the sale of merchandise to be shipped from the home state to the purchaser in his state is not "doing business" in the latter state so as to require filing incorporation papers and obtaining permission to do business.³⁷ Sale of beer in Texas to a customer does not necessarily constitute doing of business in Texas although the brewing company

³² *People's Tobacco Co. v. American Tobacco Co.*, 246 U. S. 79, 62 L. Ed. 587.

A company engaged in rebuilding and selling old automobiles is not "doing business" in a state merely because it has an agent in the state soliciting orders for such automobiles, where the orders were sent to the home office for approval and the cars delivered direct to the purchaser. *Auto Trading Co. v. Williams*, — Okla. —, 177 Pac. 583.

³³ *Hunau v. Northern Region Supply Corporation*, 262 Fed. 181.

Where an agent of a harvester company had authority only to solicit a written application from a prospective buyer and tender it, with the notes required, to the company at its home office outside the state, when, if approved, the machine would be shipped to

the purchaser, his acts as agent do not constitute doing business in the state. *Deardorf v. Idaho Nat. Harvester Co.*, 90 Ore. 425, 177 Pac. 33.

In some states, however, the taking of orders by an agent, subject to the approval of the company at its office or place of business outside the state, constitutes "doing business." *Vicksburg, S. & P. Ry. v. De Bow*, 148 Ga. 738, 98 S. E. 381, rev'g on other grounds 21 Ga. App. 732, 95 S. E. 261.

³⁴ *Alley v. Bessemer Gas Engine Co.*, 262 Fed. 94.

³⁵ *Grams v. Idaho Nat. Harvester Co.*, 105 Wash. 602, 178 Pac. 815.

³⁶ *Empire Fuel Co. v. Lyons*, 257 Fed. 890.

³⁷ *Robertson v. Southwestern Co.*, 136 Ark. 417, 206 S. W. 755.

reimbursed the buyer for rent of the premises where keg beer was stored, for money paid for advertising the beer, and furnished a truck for delivery of the beer.³⁸ So far as doing business in the state is concerned, as precluding the right of a foreign corporation to sue where it has not complied with the statutes, the corporation is not doing business in the state where it merely sells its goods to a resident to be resold by him, although he is called in the contract a "salesman," there being no agency.³⁹

§ 5924. Consignment of goods to be sold on commission.⁴⁰

§ 5925. Purchases within the state. A corporation, conducting a retail department store in Philadelphia, is "doing business" in New York, so as to be subject to the jurisdiction of its courts, where its sole manager and fifteen buyers make weekly trips to New York City to purchase goods, since "a regular and long-continued practice of buying, instead of selling, is equally doing business."⁴¹ Buying notes, contracts, choses in action, etc., in Pennsylvania, is not "doing business" therein although collections are to be made in that state by agents of the corporation to apply on the assigned accounts.⁴²

§ 5927. Soliciting traffic through traveling agents. Soliciting traffic, either freight or passenger, by an agent of a railroad company in a foreign state where its line does not run is generally held not to be the doing of business in the state, even though an office is maintained for the purpose.⁴³

³⁸ *Crisp v. Christian Moerlein Brewing Co.*, — Tex. Civ. App. —, 212 S. W. 531.

³⁹ *Shores-Mueller Co. v. Palmer*, 141 Ark. 64, 216 S. W. 295.

⁴⁰ See § 5923, *supra*.

⁴¹ *Fleischmann Const. Co. v. Blauner's*, 190 N. Y. App. Div. 95, 179 N. Y. Supp. 193.

⁴² *Finance & Guaranty Co. v. West Auburn Creamery Co.*, 69 Pa. Super. Ct. 261.

⁴³ *Graustein v. Rutland R. Co.*, 256 Fed. 409; *Davis v. Baltimore & O. R. Co.*, 256 Fed. 407; *Vicks-*

burg, S. & P. Ry. v. De Bow, 148 Ga. 738, 98 S. E. 381, *rev'g* on this ground 21 Ga. App. 732, 95 S. E. 261; *De Bow v. Vicksburg, S. & P. Ry.*, 23 Ga. App. 715, 99 S. E. 317. See also § 5932, *infra*.

A foreign railroad company is not doing business in the state, so as to be subject to the jurisdiction of the courts, merely because it has an office and agent in the state to solicit freight, especially where the cause of action had no connection with business so ini-

However, there are decisions to the contrary. Thus, it has been held that a foreign railroad company is doing business in a state, so as to be subject to suit, where it maintains an office in that state for soliciting freight and passenger business, although none of its lines are within the state.⁴⁴ So the Union Pacific Railroad Company was held to be doing business in California where it had several offices therein where passenger and freight business was solicited.⁴⁵

In any event, a railroad company having no line in Iowa is not doing business in Iowa merely because a local railroad sells tickets over its line and connecting with such foreign line, in the shape of through transportation.⁴⁶

§ 5931. Purchase and ownership of property. A foreign corporation may own and hold real estate without compliance with the statutes as to doing business in the state.⁴⁷

§ 5932. Maintaining an office or place of business in the state. The name of the corporation on the door of an office in New York City, and in a telephone and business directory, does not show a doing of business in New York.⁴⁸ A foreign railroad company having no line in Texas but having the office of the general manager and other officers in the state, from which point orders are transmitted, is not doing business in the state so as to be subject to suit for a tort committed in another state.⁴⁹

tiated. *De Bow v. Vicksburg, S. & P. Ry.*, 23 Ga. App. 715, 99 S. E. 317.

⁴⁴ *Walsh v. Atlantic Coast Line R. Co.*, 256 Fed. 47.

A Virginia railroad company is doing business in Massachusetts so as to be subject to suit there, for injury to a passenger, where it has an office to solicit business in Boston. *Walsh v. Atlantic Coast Line R. Co.*, 256 Fed. 47.

Maintaining an agent in the state to solicit freight traffic over a railroad outside the state is such a doing of business in the state as to subject it to the jurisdiction of the courts of the state,

by service of summons on such agent. *Merchants' Elevator Co. v. Chesapeake & O. Ry. Co.*, — Minn. —, 179 N. W. 734, where statute so expressly provides.

⁴⁵ *Mauser v. Union Pac. R. Co.*, 243 Fed. 274.

⁴⁶ *Jones v. Illinois Cent. R. Co.*, — Iowa —, 175 N. W. 316.

⁴⁷ *Hurst Automatic Switch & Signal Co. v. Trust Co. of St. Louis*, — Mo. —, 216 S. W. 954.

⁴⁸ *Rosenblatt v. Bridgeport Metal Goods Mfg. Co.*, 105 N. Y. Misc. 92, 173 N. Y. Supp. 331.

⁴⁹ *Atchison, T. & S. F. Ry. Co. v. Weeks*, 254 Fed. 513, recognizing conflict in decisions and rev'g

§ 5935. Institution or defense of suits not doing business. Bringing a suit for foreclosure does not constitute doing business by a foreign corporation, so as to prevent the right to sue.⁵⁰

§ 5936. Appointing agents in state. The mere presence of an agent within the state is not a doing of business.⁵¹

§ 5938. Transactions involving insurance.⁵² The mere solicitation of business by agents of a foreign insurance company, within the state, is not a doing of business in that state, so as to make the corporation subject to service of process in such state, especially where the solicitor merely forwards the premium to the head office in another state for the approval of the company.⁵³ An Iowa insurance company is not doing business in Missouri, so as to be subject to service of process, merely because it issues certificates of membership to residents of Missouri.⁵⁴ Continued existence of policies in the state after a foreign insurance company had ceased to do business in the state does not constitute doing business.⁵⁵ On the other hand, it is held that collection of premiums constitutes doing business in the state,⁵⁶ and that soliciting insurance and delivering policies in a sister state constitutes doing business in the state.⁵⁷ In

on this point, 248 Fed. 970. See also § 5927, *supra*.

⁵⁰ *Lane v. Equitable Trust Co.*, 262 Fed. 918.

⁵¹ *Rosenblatt v. Bridgeport Metal Goods Mfg. Co.*, 105 N. Y. Misc. 92, 173 N. Y. Supp. 331.

⁵² What constitutes doing business in state by insurance company, see also *American Fidelity Co. v. Leahy*, 189 N. Y. App. Div. 242, 178 N. Y. Supp. 511; *Hogan v. Empire State Surety Co.*, 8 Ohio App. 172.

What constitutes doing business by foreign fraternal benefit society, see *North American Union v. Johnson*, — Ark. —, 219 S. W. 769; *North American Union v. Oliphant*, 141 Ark. 346, 217 S. W. 1.

⁵³ *Pembleton v. Illinois Commercial Men's Ass'n*, 289 Ill. 99, 124 N. E. 355.

Solicitation of business by foreign insurance company as "engaged in business," see *Pembleton v. Illinois Commercial Men's Ass'n*, 289 Ill. 99, 124 N. E. 355, doing business in Nebraska.

⁵⁴ *Tomlinson v. Iowa State Traveling Men's Ass'n*, 251 Fed. 171.

⁵⁵ *Tucker v. Columbian Nat. Life Ins. Co.*, 232 Mass. 224, 122 N. E. 285.

⁵⁶ *Hagler v. Security Mut. Life Ins. Co.*, 244 Fed. 863.

⁵⁷ *Dixon v. Northwestern Nat. Life Ins. Co.*, — Iowa —, 179 N. W. 885.

Iowa, a nonresident insurance company does not cease to do business in another state by withdrawing its agencies and ceasing to obtain new policies if at the same time its old policies continue in force and premiums thereon are collected from the policyholders.⁵⁸

§ 5940. Miscellaneous acts held not to constitute "doing business." Sale of shares of stock is not a "doing business" by a foreign common-law corporation.⁵⁹ In Michigan a foreign corporation, where it has obtained the right to sell its stock or other securities in the state under the Blue Sky Law (Commission Act), need not comply with the Foreign Corporation Act where it desires merely to sell stock without carrying on of any business.⁶⁰

The mere soliciting and accepting advertising matter to be published in a newspaper outside the state is not "doing business" in the state.⁶¹ The fact that the by-laws of a state traveling men's association obligates all members to use their influence in favor of the association, does not make agents of members voluntarily inducing others to join, so as to make the corporation one doing business outside its home state.⁶² The mere fact that the general manager of a West Virginia company lives in Ohio, keeps a file for the company there, and conducts correspondence from that state with his corporation, does not show that the company was doing business in Ohio.⁶³ The assignment to a foreign piano company by a retail firm in California of an instalment contract of sale, where outside the ordinary business of the piano company, does not constitute doing business in the state.⁶⁴

The New York Central Railroad Company, a New York corporation, is not doing business in Ohio, so as to be subject to suit there, merely because its road is operated in connection with

⁵⁸ *Flinn v. Western Mut. Life Ass'n*, — Iowa —, 171 N. W. 711.

⁵⁹ *Home Lumber Co. v. Hopkins*, 107 Kan. 153, 190 Pac. 601.

⁶⁰ *Edward v. Ioor*, 205 Mich. 617, 172 N. W. 620.

⁶¹ *Loeb v. Star & Herald Co.*, 187 N. Y. App. Div. 175, 175 N. Y. Supp. 412.

⁶² *Tomlinson v. Iowa State Traveling Men's Ass'n*, 251 Fed. 171.

⁶³ *Empire Fuel Co. v. Lyons*, 257 Fed. 890.

⁶⁴ *W. W. Kimball Co. v. Read*, — Cal. App. —, 185 Pac. 192.

the Lake Shore road running through Ohio, and through trains are run over the two lines from New York to Chicago.⁶⁵

XV. NONCOMPLIANCE BY FOREIGN CORPORATIONS WITH STATUTES

§ 5942. Statutes merely prohibiting foreign corporations from doing business until compliance therewith.⁶⁶ In Illinois, a foreign corporation which has not complied with the conditions prescribed for transacting business in the state cannot sue in the courts of such state.⁶⁷

§ 5943. Statutes merely prescribing a penalty. Where failure to comply with statutes is made a misdemeanor by statute, contracts made by the noncomplying foreign corporation are void, it is held in Indiana.⁶⁸ The penalty section of the original Missouri act requiring foreign corporations to file a copy of their charters is not repealed by the 1909 re-enactment which is merely intended to add a clause.⁶⁹

§ 5944. Statutes merely suspending the remedy. The Missouri statute forbidding actions by foreign corporations without first complying with the statutes, means actions pertaining to business done in the state;⁷⁰ and the right to sue is not taken away by the Missouri statute for failure to have a license but only the right to enforce contracts made in the doing of business subject and contrary to state regulations.⁷¹ In that state, a foreign corporation may sue in the state for a wrong committed in derogation of its title to real estate in the state, before qualifying to do business in the state.⁷²

⁶⁵ General Inv. Co. v. Lake Shore & M. S. Ry. Co., 250 Fed. 160.

⁶⁶ Construction of New Mexico statute as to right of foreign corporation to sue in state where it has not complied with statutory requirements, see Utah Const. Co. v. St. Louis Construction & Equipment Co., 254 Fed. 321.

⁶⁷ Indiana Harbor Belt R. Co. v. Green, 289 Ill. 81, 124 N. E. 298.

⁶⁸ United States Const. Co. v.

Hamilton Nat. Bank, — Ind. App. —, 126 N. E. 866.

⁶⁹ State ex rel. Jones v. Howe Scale Co., — Mo. App. —, 218 S. W. 359.

⁷⁰ Republic Rubber Co. v. Adams, — Mo. —, 213 S. W. 80.

⁷¹ Gutta Percha Mfg. & R. Co. v. Lehrack, 201 Mo. App. 550, 214 S. W. 285.

⁷² Hurst Automatic Switch & Signal Co. v. Trust Co. of St. Louis, — Mo. —, 216 S. W. 954.

In New Hampshire the statute merely prohibits actions before complying with the local statutes, without invalidating contracts made by the foreign corporation.⁷³

§ 5945. Statutes prohibiting actions on contracts made in state before compliance. There is such a statute in New York.⁷⁴ The statutory provision in New York preventing actions by foreign corporations on a contract made in the state until a certificate is obtained, is not affected by the fact that the contract sued on was executed through the aid of a cotton exchange which was a domestic corporation.⁷⁵ Bonds or statutory undertakings, including an attachment bond, are not "contracts" which a foreign corporation is prohibited from suing on, in New York,⁷⁶ but a claim in the New York Court of Claims for additional expenses for constructing a highway for the state is an "action" within the statute.⁷⁷

A statute preventing actions by foreign corporations on contracts made in the state, for failure to comply with local laws, does not apply to contracts made out of the state; and mere signature by one of the parties in the state is immaterial.⁷⁸

§ 5946. Statutes providing that contracts made by noncomplying foreign corporations shall be absolutely void. Under the Michigan statutes, contracts of a foreign corporation which has not complied with the state statutes are void, and they cannot be allowed as claims in bankruptcy even though the bankrupt has had the benefit thereof.⁷⁹ A statute making void all contracts by unlicensed foreign corporations "relating to

⁷³ *Ensign v. Christiansen*, — N. H. —, 109 Atl. 857.

⁷⁴ The courts of New York "will not strain towards the exclusion of foreign corporations from its courts, where such exclusion will precipitate embarrassing constitutional questions." *Erie Beach Amusements v. Spirella Co.*, 105 N. Y. Misc. 170, 173 N. Y. Supp. 626.

⁷⁵ *National Cotton & Grain Co. v. Middleton*, 179 N. Y. Supp. 312.

⁷⁶ *Fairmount Film Corporation v. New Amsterdam Casualty Co.*, 189 N. Y. App. Div. 246, 178 N. Y. Supp. 525.

⁷⁷ *Amos D. Bridge's Sons, Inc. v. State*, 188 N. Y. App. Div. 500, 177 N. Y. Supp. 3.

⁷⁸ *Lehigh Structural Steel Co. v. Atlantic Smelting & Refining Works*, — N. J. Eq. —, 111 Atl. 376.

⁷⁹ *In re Springfield Realty Co.*, 257 Fed. 785.

property" within the state, does not apply to a contract to find a purchaser for property located in the state.⁸⁰

§ 5947. Statutes making contracts void in behalf of noncomplying corporation. A statute making all contracts of a foreign corporation relating to property within the state, "void on its behalf" but "enforceable against it," before compliance with state statutes, does not violate the due process of law provision, as applied to a deed to the company, although the contract was made and the deed delivered in another state.⁸¹

§ 5948. Statutes imposing a penalty, but validating contract. The penalty section in the statute requiring foreign corporations to file a copy of their charter was not repealed in Missouri by the 1909 statute.⁸²

§ 5950. Effect of retaliatory statutes upon contracts.⁸³

§ 5952. Estoppel of persons dealing with foreign corporations to assert its noncompliance with statutes. Failure of a foreign corporation to comply with statutes relating to the right to do business in the state does not authorize the other party to a contract with such a corporation to repudiate the contract.⁸⁴ A stockholder in a foreign corporation which has not complied with the local statutes does not waive any defense based on such failure to comply by his neglect to take any step to force compliance therewith by the corporation.⁸⁵

§ 5954. Estoppel of foreign corporation to assert its noncompliance with statute. The objection that a foreign corporation was not authorized to do business in the state and that therefore

⁸⁰ Charles E. Walters Co. v. Hahn, — S. D. —, 178 N. W. 448.

⁸¹ Munday v. Wisconsin Trust Co., 252 U. S. 499, 64 L. Ed. 684, aff'g Munday v. Walter, 168 Wis. 31, 168 N. W. 393, 169 N. W. 612.

⁸² State ex rel. Jones v. Howe Scale Co., — Mo. App. —, 213 S. W. 359, holding also that a judgment for the penalty does not carry interest.

⁸³ See § 5910, supra.

⁸⁴ Bradford Co. v. Dunn, 188 N. Y. App. Div. 454, 176 N. Y. Supp. 834.

⁸⁵ Lowenmeyer v. National Lumber Co., — Ind. App. —, 125 N. E. 67, where stockholder was sued by corporation to enforce specific performance of contract by him as seller of land to the company for which he received in part shares of stock.

its contracts are void cannot be urged by the corporation itself.⁸⁶ Failure of a foreign corporation to comply with the state statute as a condition of doing business makes its contracts not void but merely voidable at the option of the other party thereto.⁸⁷ A foreign corporation cannot claim that a bond given by it on removal of a cause to a federal court was invalid, for failure to comply with state statutes as to right to do business in the state, where the statute expressly provides that the corporation cannot itself take advantage of its noncompliance.⁸⁸

§ 5956. Effect of noncompliance on liability of agent to account to foreign corporation. The defense of noncompliance with the statute is available to an officer or agent of a foreign corporation who is sued by it.⁸⁹

§ 5963. Effect of contracts by noncomplying corporation having been executed. Deeds and leases made by a foreign corporation are executed transactions, and not subject to repudiation by either party because of failure of the foreign corporation to comply with the statute as to doing business.⁹⁰

§ 5964. Effect of noncompliance upon negotiable instruments executed to foreign corporation.⁹¹ A note void because of failure of the payee, a foreign corporation, to obtain a license to do business in the state, is unenforceable in the hands of an indorsee.⁹²

§ 5965. Right of assignee to enforce contract of noncomplying foreign corporation. Failure of a foreign corporation to file

⁸⁶ *Place v. Tri-State Inv. Co.*, 212 Ill. App. 524.

⁸⁷ *Yewell v. Board of Drainage Com'rs*, 187 Ky. 434, 219 S. W. 1049.

⁸⁸ *Brady v. J. B. McCrary Co.*, 244 Fed. 602, Florida statute.

⁸⁹ *King Copper Co. v. Dreher*, — Colo. —, 191 Pac. 98, which was an action to compel a corporate officer to turn over corporate books and papers; *Thomas Mfg. Co. v. Knapp*, 101 Minn. 432, 112 N. W. 989; *Billingslea Grain Co.*

v. Howell, — Tex. Civ. App. —, 205 S. W. 671.

⁹⁰ *Western U. Tel. Co. v. Louisville & N. R. Co.*, 202 Ala. 542, 81 So. 44.

⁹¹ For note on "Bona fide purchaser of negotiable paper from a foreign corporation which has not complied with the conditions of doing business in the state," see L. R. A. 1918 B 840.

⁹² *German American Bank v. Smith*, 202 Mo. App. 133, 208 S. W. 878.

its articles of incorporation, as required by statute, precludes an action in the state not only by the corporation but also by its assignee.⁹³ The statutory bar against the right to sue, for failure to comply with local statutes, applies after insolvency so as to bar an action by the receiver.⁹⁴

§ 5967. Noncompliance with statute as affecting matters not arising out of contract.⁹⁵ A noncomplying foreign corporation, although not entitled to contract, has power to bring replevin to recover its own property, replevin being a tort action.⁹⁶

§ 5969. Right of noncomplying corporation to defend action. A foreign corporation, as a defendant, may appear specially to raise the question of the jurisdiction of the court, although it has not complied with the statutes relating to such corporations.⁹⁷

§ 5971. Effect of noncompliance in federal courts.⁹⁸ If the contract is not void, prohibition against actions in the courts of the state does not prevent actions in a federal court.⁹⁹ But it is held that a foreign corporation which cannot sue in a state court for failure to comply with state requirements cannot better itself by removing the case to a federal court.¹

§ 5972. Effect of compliance after institution of suit. Filing of the articles of incorporation by a foreign corporation after the making of a contract but before an action thereon is sufficient in Arkansas under the 1907 statute, to make the contract enforceable, although the 1907 statute changed the law by making the filing after commencement of the action nugatory.²

⁹³ *Dean v. Caldwell*, 141 Ark. 38, 216 S. W. 31.

⁹⁴ *Lowenmeyer v. National Lumber Co.*, — Ind. App. —, 125 N. E. 67.

⁹⁵ See also § 5944, *supra*.

⁹⁶ *Rex Beach Pictures Co. v. Harry I. Garson Productions*, 209 Mich. 692, 177 N. W. 254.

⁹⁷ *State v. Bitter Root Val. Irrigation Co.*, 185 Iowa 60, 169 N. W. 776.

⁹⁸ See also § 5995, *infra*.

⁹⁹ *Kawin & Co. v. American Colortype Co.*, 243 Fed. 317.

¹ *Utah Const. Co. v. St. Louis Construction & Equipment Co.*, 254 Fed. 321.

² *J. R. Watkins Medical Co. v. Mosley*, 139 Ark. 294, 213 S. W. 385.

Failure to designate an agent on whom process may be served, as required by the Kentucky statutes, bars the right to sue; and a compliance pending the action is not sufficient.³ Business done by a foreign corporation prior to the issuance of a certificate of authority cannot be validated, under the Texas statutes, by subsequent issuance of the certificate.⁴

§ 5975. Alleging and proving compliance with statutory conditions.⁵ Noncompliance with state statutes as a bar to an action by a foreign corporation cannot be first urged on a motion for a new trial.⁶

§ 5978. Business which may be transacted by foreign corporation complying with statutory requirements. Compliance with the Foreign Corporations Act does not authorize a foreign corporation to sell its stock and securities without first complying with the Blue Sky Law (Commission Act).⁷

XVI. PROCEEDINGS TO EXCLUDE FOREIGN CORPORATIONS

§ 5980. In general.⁸

§ 5983. By whom ouster proceedings can be maintained. A private individual, as a taxpayer, cannot enjoin a foreign corporation from doing business in the state without compliance with statutory conditions.⁹

§ 5989. Remedies of corporation wrongfully excluded. Mandamus lies in favor of a foreign corporation to compel the

³ Hayes v. West Virginia Oil, Gas & By-Products Co., 183 Ky. 622, 210 S. W. 174.

⁴ Galveston, H. & S. A. Ry. Co. v. Hartford Fire Ins. Co., — Tex. Civ. App. —, 220 S. W. 781.

⁵ Mode of proving authority of foreign corporation to do business within state, see note in 2 A. L. R. 1235, annotating J. R. Watkins Medical Co. v. Martin, 132 Ark. 108, 2 A. L. R. 1230, 200 S. W. 238.

⁶ Watson v. Empire Cream Separator Co., 66 Colo. 284, 180 Pac. 685.

⁷ Edward v. Ioor, 205 Mich. 617, 172 N. W. 620.

⁸ Quo warranto as remedy to oust foreign corporation, see § 3232, supra.

⁹ De Peugh v. Board of Com'rs, — Ind. App. —, 126 N. E. 484.

secretary of state to deliver it a certificate authorizing it to do business in the state, where the only question involved is one of law as to the amount of the fee.¹⁰

XVII. ACTIONS BY FOREIGN CORPORATIONS

§ 5990. Right to maintain actions. A foreign corporation is not estopped to claim that it has acquired a situs as a resident of a particular county, for the purpose of suing therein, because its attorney has made an affidavit in opposing a motion, stating the corporation had no residence in the state.¹¹

§ 5993. Suit by one foreign corporation against another.¹² Foreign corporations can sue other foreign corporations on a transitory cause of action only as matter of comity.¹³

§ 5995. Noncompliance with statutes as affecting right to sue. The Missouri statute forbidding a foreign corporation or individual trustee to foreclose a deed of trust covering property in that state without joining a resident trustee as a party plaintiff does not apply to a suit in a federal court in that state by a foreign corporation.¹⁴

§ 5997. Presumption of compliance with statutory conditions. It will be presumed that a foreign corporation doing business in a state has complied with its laws,¹⁵ and hence the burden of pleading and proving noncompliance of a foreign corporation with such statutory conditions precedent, as a bar to an action by such a corporation, is on defendant.¹⁶

¹⁰ State ex rel. Bedford Coal By-Products Co. v. Fulton, 98 Ohio St. 350, 121 N. E. 697.

¹¹ Republic Motor Truck Co. v. Buda Co., 212 Mich. 55, 179 N. W. 474.

¹² Venue, see § 6013, *infra*.

¹³ Arizona Commercial Min. Co. v. Iron Cap Copper Co., 233 Mass. 522, 124 N. E. 281, where court refused to entertain the suit for various reasons.

¹⁴ Lane v. Equitable Trust Co., 262 Fed. 918.

¹⁵ Western U. Tel. Co. v. Louisville & N. R. Co., 202 Ala. 542, 81 So. 44.

¹⁶ W. W. Kimball Co. v. Read, — Cal. App. —, 185 Pac. 192; Northern Counties Land Co. v. Excelsior Land, Mining & Development Co., — Minn. —, 178 N. W. 497; Brioschi-Minuti Co. v. Elson-Williams Const. Co., — N. D. —, 172 N. W. 239.

§ 5998. Manner of raising defense of noncompliance by foreign corporation. Allegation in a complaint of compliance by plaintiff, a foreign corporation, with statutory requirements, cannot be denied on information and belief.¹⁷ A merely general allegation of failure to comply with the tax law is bad as a conclusion of law.¹⁸ One sued by a foreign corporation, who sets up the defense that the corporation has not complied with statutory conditions precedent to the transaction "of any business within this state," must show by his plea that the corporation was transacting business within the state.¹⁹

§ 6004. Necessity of pleading charter or corporate powers. A foreign corporation need not set out in its charter, to show its capacity to sue.²⁰

XVIII. ACTIONS AGAINST FOREIGN CORPORATIONS

§ 6005. In general. In one case it is said that in the absence of legislative enactment, a corporation cannot be sued outside the state where it was created.²¹ A proceeding against a foreign corporation to recover a penalty for a violation of a statute is a civil action and not a criminal one.²² A foreign express company licensed to do business in the state is a resident of a county where it has an agent and is sued and served with process through the agent, for the purposes of appealing from the decision of a justice of the peace, under the Missouri statutes.²³

§ 6006. Requisites to jurisdiction to render personal judgment against foreign corporation. A personal judgment cannot be rendered against a foreign corporation unless it volun-

¹⁷ *Art Metal Const. Co. v. A. F. Anderson Co.*, — Cal. —, 186 Pac. 776.

¹⁸ *Fairmount Film Corporation v. New Amsterdam Casualty Co.*, 189 N. Y. App. Div. 246, 178 N. Y. Supp. 525.

¹⁹ *Brioschi-Minuti Co v. Elson-Williams Const. Co.*, — N. D. —, 172 N. W. 239.

²⁰ *Bass v. African Methodist Episcopal Church*, —Ga. —, 104 S. E. 437.

²¹ *Folkes v. Central of Georgia R. Co.*, 202 Ala. 376, 80 So. 458, citing *Pullman Palace Car Co. v. Harrison*, 122 Ala. 149, 82 Am. St. Rep. 68, 25 So. 697.

²² *State ex rel. Jones v. Howe Scale Co.*, 277 Mo. 213, 210 S. W. 8.

²³ *Hartell v. American Ry. Express Co.*, — Mo. App. —, 225 S. W. 131.

tarily appears or has been doing business within the state.²⁴ The liability of a foreign corporation to be sued does not depend on the situs or character of the business out of which the litigation arises but on the presence of the corporation, i. e., the doing of business.²⁵ A foreign corporation sued on a fidelity bond in a state where it is doing business cannot defend on the ground that the defrauding employees were nonresidents and necessary parties.²⁶

The Washington statute making a foreign corporation subject to actions on contracts, after it has ceased to exist as an entity under the Washington laws, applies only when the cause of action accrued prior to the withdrawal from the state.²⁷

§ 6007. Who may maintain suit against foreign corporation.

The North Carolina statute, copied from the New York statute, as to the venue of actions against foreign corporations, does not preclude an action in that state on a transitory cause of action, by a nonresident against a foreign corporation, on a cause of action arising out of the state.²⁸

§ 6008. Actions which may be brought against foreign corporations. A nonresident may sue a foreign corporation on a transitory cause of action anywhere it can be found.²⁹ A foreign corporation may be sued on a transitory cause of action arising outside the state, where doing business in the state and duly served with process.³⁰ Under the New York statute, service on the designated agent of a foreign corporation is good although the cause of action arose in another state;³¹ but under such statute, a foreign corporation cannot be sued in New York, after

²⁴ Vicksburg, S. & P. Ry. v. De Bow, 148 Ga. 738, 98 S. E. 381, rev'g on other grounds 21 Ga. App. 732, 95 S. E. 261; De Bow v. Vicksburg, S. & P. Ry., 23 Ga. App. 715, 99 S. E. 317.

²⁵ Walsh v. Atlantic Coast Line R. Co., 256 Fed. 47.

²⁶ Ransburg v. United States Fidelity & Guaranty Co., — Ind. App. —, 124 N. E. 765.

²⁷ Gerriek & Gerriek Co. v.

Llewellyn Iron Works, 105 Wash. 98, 177 Pac. 692, and see § 6046, *infra*.

²⁸ Ledford v. Western U. Tel. Co., 179 N. C. 63, 101 S. E. 533.

²⁹ Ledford v. Western U. Tel. Co., 179 N. C. 63, 101 S. E. 533.

³⁰ Atchison, T. & S. F. Ry. Co. v. Weeks, 248 Fed. 970.

³¹ Philadelphia & Reading Coal & Iron Co. v. Kever, 260 Fed. 534.

If the cause of action against a

it has ceased to do business therein, on a cause of action arising in another state, although the designation of an agent to receive service of process has not been revoked.³²

§ 6009. Jurisdiction—Federal courts. A foreign corporation may be sued in the federal courts as a nonresident.³³

§ 6012. Effect of appearance. Appearance by a foreign corporation submits itself to the jurisdiction of the court.³⁴ An appearance by a foreign corporation merely to attack the service on the ground that a proper person was not served is a special appearance.³⁵ A plea or motion filed by a defendant foreign corporation, setting up that it was not and never had been transacting business in the state, is not a plea to the merits, and hence is a special rather than a general appearance.³⁶

§ 6013. Venue. A constitutional provision as to the counties in which a foreign corporation may be sued does not deprive the legislature of power to provide for additional places where such corporations may be sued.³⁷ A foreign corporation, by compliance with the statutes, acquires no county residence, within the venue statutes.³⁸ A foreign railroad company is properly sued for a tort in the county through which its road ran, although an individual defendant resided in another county.³⁹

foreign corporation arises outside New York, there is no jurisdiction in the New York courts unless the corporation has property in New York. *Loeb v. Star & Herald Co.*, 187 N. Y. App. Div. 175, 175 N. Y. Supp. 412.

³² *Chipman v. Thomas B. Jeffery Co.*, 260 Fed. 856.

³³ *Folkes v. Central of Georgia R. Co.*, 202 Ala. 376, 80 So. 458.

³⁴ *Davis v. Central New Hampshire Power Co. of Maine*, — N. H. —, 109 Atl. 263.

³⁵ *Kluver v. Midwest Grain Co.*, — N. D. —, 173 N. W. 468.

³⁶ *State v. Bitter Root Val. Irrigation Co.*, 185 Iowa 60, 169 N. W. 776.

³⁷ *Prairie Oil & Gas Co. v. District Court*, — Okla. —, 174 Pac. 1056.

³⁸ *Pekin Cooperage Co. v. Duty*, 140 Ark. 135, 215 S. W. 715; *Ryan v. Inyo Cerro Gordo Mining & Power Co.*, — Cal. App. —, 183 Pac. 250.

A foreign corporation doing business in California does not establish a residence in any particular county, such as is contemplated by the statutes relating to place of trial. *Ryan v. Inyo Cerro Gordo Mining & Power Co.*, — Cal. App. —, 183 Pac. 250.

³⁹ *Smyer v. Southern R. Co.*, 110 S. C. 292, 96 S. E. 483.

A foreign corporation which has complied with the Michigan statutes has the situs of domestic corporations for jurisdictional purposes so as to be authorized to sue in the county of its principal place of business for breach of contract by another foreign corporation.⁴⁰

In many states special statutes fix the venue of actions against foreign corporations.⁴¹ In Arkansas a foreign corporation may be sued in a county where it has a branch office or place of business.⁴² In California, compliance with the statutes relating to foreign corporations does not give a foreign corporation a residence in the state nor give it the rights of a domestic corporation in regard to the place of trial of actions; and a foreign corporation is not entitled to have an action against it for personal injuries tried in the county where the injuries occurred.⁴³ The Iowa statute provides that when a corporation has "an office or agency in any county for the transactions of business," any actions "growing out of or connected with the business of that office or agency may be brought in the county where such office or agency is located." Thereunder, where a foreign corporation had its main office in one county and sued its agent at its office in another county, the agent could not sue for malicious prosecution in the latter county.⁴⁴ In Missouri, a foreign insurance company is suable either in the county where the cause of action accrued or in any county where such foreign corporation has an agent for the transaction of its usual and customary business.⁴⁵ In Texas, an action against a foreign corporation may be brought in a county where it has an agent; and it is immaterial that it was agreed that such agent was to have no authority to accept or receive service of process.⁴⁶

⁴⁰ Republic Motor Truck Co. v. Buda Co., 212 Mich. 55, 179 N. W. 474.

⁴¹ See Prairie Oil & Gas Co. v. District Court, — Okla. —, 174 Pac. 1056, and also vol. 1, § 397.

Venue of actions against foreign insurance corporations, under Kansas statutes, see Nowak v. Bankers' Life Ins. Co., 103 Kan. 778, 176 Pac. 654.

⁴² Ft. Smith Iron & Steel Mills v. Southern Round Bale Press Co.,

139 Ark. 101, 213 S. W. 21.

⁴³ Ryan v. Inyo Cerro Gordo Mining & Power Co., — Cal. App. —, 183 Pac. 250.

⁴⁴ Ewing v. Hawkeye Oil Co., — Iowa —, 174 N. W. 942, distinguishing Locke v. Chicago Chronicle, 107 Iowa 390, 78 N. W. 49.

⁴⁵ State ex rel. Standard Fire Ins. Co. of Hartford v. Gantt, 274 Mo. 490, 203 S. W. 964.

⁴⁶ Advance-Rumely Thresher Co. v. Moss, — Tex. Civ. App. —,

Under the federal statute providing that where jurisdiction is founded on diversity of citizenship, suit shall be brought in the district of the residence of either the plaintiff or defendant, a foreign corporation has no residence outside the state of its creation.⁴⁷ A suit by one foreign corporation against another to enjoin a breach of contract to deliver gas in the state where suit is brought is not a "local suit" or one to "enforce a lien upon or claim to property" within the district, within the federal statutes, so as to authorize a bringing of the suit in the district where both parties are nonresidents.⁴⁸

§ 6014. Right of foreign corporation to defend suit against it.⁴⁹

§ 6015. Right of foreign corporation to assert as a defense noncompliance with statutory requirements.⁵⁰

§ 6016. Pleadings in actions against foreign corporations.⁵¹
The defense that defendant is a foreign corporation not subject to the jurisdiction of the court because not doing business in the state should be raised by plea in abatement rather than by motion to quash.⁵²

§ 6017. Statute of limitations and laches as a defense.⁵³

XIX. SERVICE OF PROCESS ON FOREIGN CORPORATIONS

§ 6020. Consent to prescribed manner of service implied from doing business in state. A nonresident insurance company doing business in Iowa will be conclusively presumed to have complied with the statute requiring the filing of an agreement that service of process may be made on the state auditor.⁵⁴

213 S. W. 690. See also *Atchison, T. & S. F. R. Co. v. Stevens*, 109 Tex. 262, 206 S. W. 921, aff'g — Tex. Civ. App. —, 192 S. W. 304.

⁴⁷ *McCullough v. United Grocers' Corporation*, 247 Fed. 880, and see *Fletcher Cyc. Corp.* § 396.

⁴⁸ *Kansas Gas & Electric Co. v. Wichita Natural Gas Co.*, 266 Fed. 614.

⁴⁹ See § 5969, *supra*.

⁵⁰ See §§ 5953, 5954, *supra*.

⁵¹ See also § 3082, *supra*.

⁵² *Daniels v. Yarhola Pipe Line Co.*, — Mo. App. —, 206 S. W. 600.

⁵³ See § 398, *supra*.

⁵⁴ *Flinn v. Western Mut. Life Ass'n*, — Iowa —, 171 N. W. 711.

§ 6021. Doing business essential to jurisdiction in personam.⁵⁵

A foreign corporation is not subject to service of process unless doing business within the state,⁵⁶ and a state statute relating to service of process is not applicable to a foreign corporation not doing business in the state.⁵⁷ A state statute making agents for the service of process on, any person receiving money on account of any contract of insurance, does not apply to a foreign corporation soliciting insurance by agents where not, legally speaking, doing business in the state.⁵⁸ Residence of the president of a foreign corporation in the state, where it is not doing business in the state, does not authorize service of process on him.⁵⁹ In New York, the unrevoked designation by a foreign corporation of a person on whom process may be served does not make the corporation subject to suit in New York after it has removed from the state, where the cause of action arose outside of the state.⁶⁰

⁵⁵ Note on "Right to serve process on public officer or designated agent of foreign corporation in action arising out of transaction in another state," see Ann. Cas. 1918 A 392.

⁵⁶ Davenport v. Superior Court, — Cal. —, 191 Pac. 911; Pembleton v. Illinois Commercial Men's Ass'n, 289 Ill. 99, 124 N. E. 355; Jones v. Illinois Cent. R. Co., — Iowa —, 175 N. W. 316.

A foreign corporation cannot be served with process in a state where it is not doing business, has no property, and where it has appointed no agent to accept service. Pine Hill Coal Co. v. Gusicki, 261 Fed. 974.

Where a foreign corporation is not doing business in the state, and has never filed with the state auditor written authority for him to accept service for it, service of a summons on the deputy state auditor is not service on the corporation. Schwabe v. American Rural Credits Ass'n, — Neb. —, 175 N. W. 673.

Service of summons cannot be made in the state where the company is doing business in the state only by a salesman who maintains an office therein and merely takes orders subject to confirmation by and shipped from the home office. Foreign Products Co. v. C. C. Mengel & Bro. Co., 193 N. Y. App. Div. 951, 184 N. Y. Supp. 457, following Beck v. North Packing & Provision Co., 159 N. Y. App. Div. 418, 144 N. Y. Supp. 602.

What constitutes doing business in state, see §§ 5916-5940, supra.

⁵⁷ Pembleton v. Illinois Commercial Men's Ass'n, 289 Ill. 99, 124 N. E. 355, Nebraska statute.

⁵⁸ Pembleton v. Illinois Commercial Men's Ass'n, 289 Ill. 99, 124 N. E. 355.

⁵⁹ Wollman v. Newark Star Pub. Co., 190 N. Y. App. Div. 933, 179 N. Y. Supp. 899.

⁶⁰ Chipman v. Thomas B. Jeffrey Co., 251 U. S. 373, 64 L. Ed. 314, aff'g 260 Fed. 856.

§ 6023. Service on foreign corporation engaged in interstate commerce. The statute requiring filing of the name of an agent on whom process may be served does not apply to corporations engaged in interstate commerce.⁶¹

§ 6025. Place of making service. A statute is constitutional which permits service on agents of foreign corporations in any county including counties outside the county where the action is brought or pending.⁶² Statutes providing that service of summons may be made upon an agent of a foreign corporation at any place within the state is not unconstitutional as discriminating against foreign corporations nor as violating the Fourteenth Amendment of the Federal Constitution.⁶³

§ 6030. Upon whom process may be served generally.⁶⁴ An agent of a foreign corporation cannot be served with process unless his authority and the business in which he is engaged is of such a character that it may be said that, in his person, the corporation is there present; but an agent authorized to take orders, make adjustments, and dispose of corporate property within the state is such an agent.⁶⁵ Summons cannot be served on an employee whose duties are purely mechanical such as installing an engine.⁶⁶ Of course, service cannot be made on a resident broker who had never been an agent of the foreign corporation.⁶⁷ An agent of a local railroad company is not subject to service of process as agent of a foreign railroad company because the former sells tickets with coupons over the latter road, as a through ticket.⁶⁸ Under the Nebraska statutes as to service of insurance companies, any person who with authority receives or receipts for money from other persons to

⁶¹ Reichert v. Ellis Ferry Co., 184 Ky. 150, 211 S. W. 403.

⁶² Pekin Cooperage Co. v. Duty, 140 Ark. 135, 215 S. W. 715.

⁶³ Pekin Cooperage Co. v. Duty, 140 Ark. 135, 215 S. W. 715.

⁶⁴ Persons held "agents" of foreign corporation subject to be served with process, see Grams v. Idaho Nat. Harvester Co., 105 Wash. 602, 178 Pac. 815.

⁶⁵ Nienhauser v. Robertson Paper Co., — Minn. —, 178 N. W. 504.

⁶⁶ Alaska Pacific Nav. Co. v. Southwark Foundry & Machine Co., 104 Wash. 346, 176 Pac. 357.

⁶⁷ Atlantic & Gulf Grocery Co. v. Aetna Mills Co., 77 Fla. 113, 80 So. 738.

⁶⁸ Jones v. Illinois Cent. R. Co., — Iowa —, 175 N. W. 316.

be remitted to the company for a policy is deemed an agent on whom process may be served.⁶⁹ In case of a foreign surety company, coming within the class of foreign insurance companies, service of process must be made, under the Mississippi statute, on the agent appointed as required by statute.⁷⁰

Service of process on a domestic corporation as the agent of a foreign corporation is authorized where it in fact acts as an agent although the contract under which it acts expressly provides that it should not be construed as creating an agency.⁷¹ Service of process cannot be made on a domestic corporation as the agent or substitute for a foreign corporation merely because most or all of the stock of the domestic company is owned by the foreign company.⁷² Service of process on a foreign corporation as agent of another foreign corporation is proper where the agent might have been served if an individual.⁷³

Declarations of the person served or of any other person in the office are not binding on the corporation to show that the person served was such an agent of a foreign corporation as could be legally served.⁷⁴

§ 6031. Exclusiveness of statutory method of service. A statute providing that process against a foreign insurance company "may" be served on the insurance commissioner is not exclusive.⁷⁵

§ 6033. Service upon designated state official. The statute authorizing service of summons, in actions against foreign corporations, on the corporation commissioner, does not apply to a corporation which had withdrawn from the state several years before the statute was enacted.⁷⁶ In Kansas service on the

⁶⁹ *Crews v. Illinois Commercial Men's Ass'n*, 256 Fed. 268, holding that isolated act of transferring money did not continue agency after acceptance of money.

⁷⁰ *National Surety Co. v. Board Sup'rs Holmes County*, 120 Miss. 706, 83 So. 8.

⁷¹ *McNeill v. Electric Storage Battery Co.*, 109 S. C. 326, 96 S. E. 134.

⁷² *Atchison, T. & S. F. Ry. Co. v. Weeks*, 248 Fed. 970.

⁷³ *Calhoun Mills v. Black Diamond Collieries*, 112 S. C. 332, 99 S. E. 821.

⁷⁴ *Loeb v. Star & Herald Co.*, 187 N. Y. App. Div. 175, 175 N. Y. Supp. 412.

⁷⁵ *Carr v. Aetna Accident & Liability Co.*, 263 Pa. 87, 106 Atl. 107, rev'g 64 Pa. Super. Ct. 343.

⁷⁶ *Beedle v. Stoddall Land & Timber Co.*, 96 Ore. 590, 189 Pac. 427.

superintendent of insurance is allowed only where the action is brought in the county in which plaintiff resides or the county in which the cause of action arose.⁷⁷ Where a foreign insurance corporation is doing business in Arkansas without compliance with local statutes, it is estopped to deny that the superintendent of insurance was its agent for service of process.⁷⁸ If service on a foreign insurance company is required to be made on the state auditor, service may be made on the commissioner of insurance where a later statute provides that the powers and duties of the auditor relating to insurance shall be vested in the commissioner of insurance.⁷⁹

§ 6035. Service on "managing agent," "superintendent," etc., other than executive officers. A mere office employee of a foreign corporation which purchases goods in New York City, who has no discretion and merely keeps the company advised as to market conditions, is not a "general manager" who may be served with process.⁸⁰ The private secretary of an advertising solicitor is not a "managing agent" who may be served.⁸¹ That one assumed to act as managing agent does not make him a proper person to serve, unless he was authorized by the corporation to so act.⁸² The fact that an agent of a foreign corporation is paid by a commission does not preclude his being a "business agent" on whom process may be served.⁸³ Where a federal statute provides for service of process on the resident agent of a foreign surety company or upon the clerk of the district court, substituted service on the resident agent is not sufficient.⁸⁴

⁷⁷ *Shearer v. Farmers' Life Ins. Co.*, 106 Kan. 574, 189 Pac. 648.

⁷⁸ *North American Union v. Oliphant*, 141 Ark. 346, 217 S. W. 1.

⁷⁹ *Flinn v. Western Mut. Life Ass'n*, — Iowa —, 171 N. W. 711.

⁸⁰ *Metropolitan Bank of New York v. Baker, Hamilton & Pacific Co.*, 178 N. Y. Supp. 140.

⁸¹ *Loeb v. Star & Herald Co.*, 187 N. Y. App. Div. 175, 175 N. Y. Supp. 412.

⁸² *Loeb v. Star & Herald Co.*, 187 N. Y. App. Div. 175, 175 N. Y. Supp. 412.

⁸³ *Charles Ehrlich & Co. v. J. Ellis Slater Co.*, — Cal. —, 192 Pac. 526.

Who is "business agent," under California statute, see also *Knapp v. Bullock Tractor Co.*, 242 Fed. 543.

⁸⁴ *United States ex rel. Yarnell v. Southern Dredging Co.*, 251 Fed. 400.

§ 6040. Service on local agent. A "local" agent of a foreign corporation, subject to be served with process under the Texas statutes, is "an agent at a given place or within a district."⁸⁵

§ 6041. Service on officer casually or temporarily in state. A conductor of a railroad company cannot be served with process as its agent where he performs no services for the company in the state.⁸⁶

§ 6045. Effect of termination of agency on service. One who has ceased to represent a foreign corporation as its agent cannot be served with process.⁸⁷ Unless otherwise provided by statute, service cannot be made on a statutory agent designated as such for service of process, after he had left the company, although the designation was not formally revoked.⁸⁸ In New York, if the person designated as agent on whom process may be served, revokes his appointment, service may still be made on the secretary of state.⁸⁹ Revocation of the appointment of an agent to receive service of process is valid although not sanctioned by formal action of the board of directors.⁹⁰

§ 6046. Effect of withdrawal of corporation from the state. Under the New York law, where a foreign corporation appoints an agent on whom process may be served, and then removes from the state, service on the agent is invalid in an action on a contract made and to be performed in another state, where no act of breach or performance was done in New York.⁹¹ After a

⁸⁵ *Alley v. Bessemer Gas Engine Co.*, 262 Fed. 94.

⁸⁶ *Atchison, T. & S. F. Ry. Co. v. Weeks*, 248 Fed. 970.

⁸⁷ *State v. Bitter Root Val. Irrigation Co.*, 185 Iowa 60, 169 N. W. 776; *Kluver v. Middlewest Grain Co.*, — N. D. —, 173 N. W. 468.

⁸⁸ *Gerrick & Gerrick Co. v. Llewellyn Iron Works*, 105 Wash. 98, 177 Pac. 692.

⁸⁹ *Saxe v. Sugarland Mfg. Co.*, 189 N. Y. App. Div. 204, 178 N. Y. Supp. 454.

⁹⁰ *People's Tobacco Co. v. American Tobacco Co.*, 246 U. S. 79, 62 L. Ed. 587.

⁹¹ *Chipman v. Thomas B. Jeffery Co.*, 251 U. S. 373, 64 L. Ed. 314, aff'g 260 Fed. 856, holding that under the New York statutes requiring foreign corporations to designate an agent on whom service may be made, service on such an agent is not good where the cause of action arose after the corporation ceased to do business in the state.

foreign corporation has surrendered authority to do business in New York, it cannot be served with process unless the action is to enforce a liability incurred prior to the filing of the surrender.⁹² Service of summons on the secretary of state and the local agent designated by a foreign corporation is not effective where made after the corporation had withdrawn from the state, the agency had ceased, and the corporation had been declared nonexistent for nonpayment of license fees.⁹³

Where a subsidiary corporation amounts to but little more than a bookkeeping arrangement, created on withdrawal of the parent foreign corporation from a state, and all the subsequent deals are conducted with the local agent of the subsidiary rather than its officers, the filing of notice of withdrawal from the state does not prevent service of process on it in such state.⁹⁴

§ 6051. Service in suits in federal courts. The state law governs as to who may be served with process, in an action in a federal court against a foreign corporation.⁹⁵

§ 6056. Acceptance of service by agent. A statute permitting "acceptance" of service by the state auditor, in actions against foreign insurance companies, does not require an acceptance of service, where service is actually made on the auditor.⁹⁶

⁹² *Hexter v. Day-Elder Motors Co.*, 192 N. Y. App. Div. 394, 182 N. Y. Supp. 717.

⁹³ *Gerrick & Gerrick Co. v. Llewellyn Iron Works*, 105 Wash. 98, 177 Pac. 692.

⁹⁴ *Cutler v. Cutler-Hammer Mfg. Co.*, 266 Fed. 388.

⁹⁵ *Walsh v. Atlantic Coast Line R. Co.*, 256 Fed. 47.

If a foreign corporation is doing business in the district, service on it is sufficient in the federal courts where it would be valid under the state law. *Walsh v. Atlantic Coast Line R. Co.*, 256 Fed. 47.

⁹⁶ *Flinn v. Western Mut. Life Ass'n*, — Iowa —, 171 N. W. 711.

CHAPTER 66

MASSACHUSETTS TRUSTS AND KINDRED ASSOCIATIONS

- § 6059. Definition and nature—In general.
- § 6061. — Agreement as constituting partnership.
- § 6063. Reasons and advantages of trust instead of corporation.
- § 6067. Form and contents of trust agreements.
- § 6086. Shares and certificates of stock.
- § 6091. Duration and termination of trust.
- § 6095. Rights, powers and duties of trustees—Liability on contracts.
- § 6103. — Actions by or against trustee.
- § 6115. Taxation.

§ 6059. Definition and nature—In general.¹ The agreement of trust creates a voluntary association with a collective title.² A trust under which the trustees are to carry on a manufacturing business is essentially different from an ordinary real estate trust of the kind familiar in Massachusetts.³ A common-law corporation, in the form of an unincorporated trust, having powers and privileges not possessed by individuals or partnerships, is, by constitutional provision, within the term "corporations" as used in the article relating to the right to sell stock.⁴

§ 6061. — Agreement as constituting partnership. The test to determine whether an association is a trust or a partnership is the power of control. If the certificate holders have the power of control, it is a partnership; if the trustee has the power it is a trust.⁵ Where the articles of association provide that a meet-

¹ See *Bingham v. Graham*, — Tex. Civ. App. —, 220 S. W. 105; *Oil Lease & Royalty Syndicate v. Beeler*, — Tex. Civ. App. —, 217 S. W. 1054.

For article on nature of Massachusetts business trusts, see 27 Yale L. J. 677-683. See also note in 7 A. L. R. 612.

² See *Adams v. Swig*, — Mass. —, 125 N. E. 857.

³ *Malley v. Bowditch*, 259 Fed. 809, 7 A. L. R. 608.

⁴ *Home Lumber Co. v. Hopkins*, 107 Kan. 153, 190 Pac. 601, and see § 16, *supra*.

⁵ *Simson v. Klipstein*, 262 Fed. 823.

ing of the certificate holders may be called at any time and that they may amend any and all of the articles of association except in minor matters, the association is a partnership and not a trust; and it is not necessary that the power of control be actually exercised to constitute a partnership.⁶ Where trustees are given exclusive management and control, and the shareholders have no voice in the management and no right even to call for an accounting by the trustees, the association is not a partnership but a trust.⁷ Where shareholders have no control over the trustees and persons dealing with the trustees can look only to the trust property for satisfaction, the agreement creates a trust rather than a partnership.⁸

§ 6063. Reasons and advantages of trust instead of corporation.⁹

§ 6067. Form and contents of trust agreements.¹⁰

§ 6086. Shares and certificates of stock. The words "certificates of stock" as used in a statute may apply to certificates in a trust.¹¹ A Massachusetts trust is an association "having powers and privileges not possessed by individuals or partnerships," so as to be within the Blue Sky Law so far as the right to sell its stock is concerned.¹² An application by a foreign common-law corporation for leave to sell securities and stock in the state, under the Blue Sky Law, should be considered and passed on according to the merits.¹³

For illustration of agreement of association held a trust rather than a partnership, see *Davis v. Hudgins*, — Tex. Civ. App. —, 225 S. W. 73, citing *Bingham v. Graham*, — Tex. Civ. App. —, 220 S. W. 105.

⁶ *Simson v. Klipstein*, 262 Fed. 823.

⁷ *Home Lumber Co. v. Hopkins*, 107 Kan. 153, 190 Pac. 601.

⁸ *Home Lumber Co. v. Hopkins*, 107 Kan. 153, 190 Pac. 601, reviewing the decisions at length.

⁹ Article on common-law trusts

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superseding private corporations, see 53 Am. L. Rev. 759-761; 89 Cent. L. J. 275-277. Article on passing of the corporation in business, see 2 Minn. L. Rev. 401-414.

¹⁰ For form of trust agreement, see *Adams v. Swig*, — Mass. —, 125 N. E. 857.

¹¹ *Malley v. Bowditch*, 259 Fed. 809, 7 A. L. R. 608.

¹² *Home Lumber Co. v. Hopkins*, 107 Kan. 153, 190 Pac. 601.

¹³ *Home Lumber Co. v. Hopkins*, 107 Kan. 153, 190 Pac. 601.

§ 6091. Duration and termination of trust. The appointment of a receiver for a common-law corporation is governed, it seems, by the same general rules applicable to ordinary corporations.¹⁴

§ 6095. Rights, powers and duties of trustees—Liability on contracts. So far as the signatures of trustees to corporate paper are concerned, the question of their personal liability is governed by the same rules applicable to corporations proper.¹⁵ Trustees who sign a note “National Realty Co., By Simon Swig, Edward L. McManus, Trustees” are not individually liable where the association existed and they had power to act.¹⁶

§ 6103. — Actions by or against trustee. If the agreement constitutes a trust rather than a partnership, all the stockholders need not be made parties to an action by some of the beneficiaries against the trustees for breach of trust.¹⁷

§ 6115. Taxation. The federal statute imposing a stamp tax on certificates of stock applies equally well to certificates of shares issued by a trust organized as a common-law corporation.¹⁸ The stamp tax on certificates of stock is not unconstitutional, as applied to a trust to manage a manufacturing plant, because not applicable to other associations issuing no muniments of title.¹⁹

¹⁴ Davis v. Hudgins, — Tex. Civ. App. —, 225 S. W. 73.

¹⁵ See Adams v. Swig, — Mass. —, 125 N. E. 857.

¹⁶ Adams v. Swig, — Mass. —, 125 N. E. 857.

¹⁷ Davis v. Hudgins, — Tex. Civ. App. —, 225 S. W. 73.

¹⁸ Malley v. Bowditch, 259 Fed. 809, 7 A. L. R. 608.

¹⁹ Malley v. Bowditch, 259 Fed. 809, 7 A. L. R. 608.

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